No. 83-27

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

AXEL N. ELIASEN, on behalf of himself and all others similarly situated,

Petitioner,

v.

GREEN BAY & WESTERN RAILROAD COMPANY, H. WELDON McGEE, R. B. WILSON, JOHN WINTHROP, and CHARLES W. COX, II,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

I. In a case involving self-dealing by corporate directors, whether a prior State Supreme Court holding that the holders of certain corporate securities are "on the footing of shareholders of an ordinary corporation" as "the owners of the equity of the corporation" is not preclusive for purposes of *res judicata* on the grounds that the prior case "only" considered rights to annual income?

II. Whether corporate directors, in determining the form of the transaction under which their corporation will be taken over, have a fiduciary duty to protect the interests of investors holding non-voting equity securities?

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PARTIES TO PROCEEDINGS BELOW

The petitioner, Axel N. Eliasen, is the certified class representative of all holders of Class B debentures of the respondent, Green Bay & Western Railroad, as of November 29, 1977, excluding members of the board of directors and persons and entities holding debentures for the benefit of directors or members of their families. Three intervenors below, William J. Urban, Charles J. VerHalen, and the Estate of Paul Sperling, are class members whose interests are represented by petitioner. The caption of this case includes the names of all respondents, both the Railroad and its directors at that time.

REPORTS OF OPINIONS BELOW

The opinion of the District Court (Appendix 1a-26a) and the order of the Court of Appeals (Appendix 27a) have not been reported in any official or unofficial reports. The District Court's decision granting class action status is reported at 93 F.R.D. 408 (1982).

GROUNDS OF JURISDICTION

This case was commenced in the United States District Court for the Eastern District of Wisconsin, which had jurisdiction under 28 U.S.C. §1332; petitioner was certified as the class representative under the provisions of Rule 23(b)(1), Fed. R. Civ. P. From an Opinion and Judgment entered September 13, 1982 granting summary judgment of dismissal, petitioner appealed to the United States Court of Appeals for the Seventh Circuit pursuant to 28 U.S.C. §1291; the Court of Appeals entered an unpublished order affirming judgment and adopting the District Court's opinion as its own on March 11, 1983. Petitioner filed a petition for a rehearing, which was denied by order dated April 14, 1983. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

AUTHORITIES OF LAW INVOLVED

These proceedings do not involve the construction of any statutes, contracts or the like; however, these proceedings involve the construction of a prior decision of the Supreme Court of Wisconsin in *Biltchik v. Green Bay & Western Railroad,* 250 Wis. 177, *cert. denied* 332 U.S. 835 (1947), reproduced at Appendix 29a-36a. To the extent the case involves construction of the B debentures of the Green Bay & Western Railroad, the pertinent provisions are quoted therein.

STATEMENT OF THE CASE

Both before and during the pendency of this case, the rights of holders of the B debentures of the Green Bay & Western Railroad Company (hereinafter GB&W) have been the subject of substantial litigation. The GB&W was incorporated in 1896 pursuant to a plan of reorganization instituted in connection with foreclosure proceedings against a prior railroad. The GB&W's initial capitalization consisted of $600,000 face amount of Class A debentures issued in exchange for cash, $2,500,000 par value capital stock issued in exchange for old first mortgage bonds, and $7,000,000 face amount of B debentures issued in exchange for common stock in the prior railroad. All securities have been publicly traded. Because this case raises issues of *res judicata,* it is necessary to consider the prior litigation in some detail.

A. Prior Litigation.

The first litigation involved the claim of the GB&W that amounts paid to the holders of its debentures were deductible as interest under the income tax laws. In deciding this issue, the Court of Appeals and the Tax Court concluded that the B debentures were part of the capitalization of the GB&W and that all payments of them were subject and inferior to payments on A debentures and the capital stock. *Green Bay & W. R. Co. v. C. I. R.*, 147 F.2d 585, 586, 587 (7th Cir. 1945) *aff'g* 3 T.C. 372 (1944). These decisions were based upon the construction of the language of the debentures and the facts relating to their initial issuance.

During the pendency of the tax case, three holders of B debentures commenced a class action against the GB&W in the U.S. District Court for the Southern District of New York, asserting that the holders of B debentures were entitled to the distribution of all annual net earnings of the corporation not

distributed to holders of A debentures and capital stock. This action was initially dismissed under the doctrine of *forum non conveniens*. *Williams v. Green Bay & Western R. Co.*, 147 F.2d 777 (2nd Cir. 1945), *aff'g* 59 F.Supp. 98. The B debenture holders petitioned this Court for a Writ of Certiorari, which was granted.

The *Williams* case was initially filed during the October, 1944 term of this Court (file number 1335). In Respondent's Brief in Opposition to Petition for Writ of Certiorari, the GB&W succinctly stated:

> "The facts are that the Class B debentures are a very unusual type of security, the junior equity security issued by the respondent, a position normally occupied by common stock. The Class B debentures are junior to the Class A debentures and the so-called Common Stock. In the event of reorganization or sale, which is the only maturity date of the debentures, the holders are entitled to everything remaining after payment of the face amount of the Class A debentures ($600,000) and the Common Stock ($2,500,000). Therefore, all restrictions on distributions of annual earnings deemed necessary for the best interests of the Railroad operate to the ultimate benefit of the holders of the Class B debentures. . . .
>
> "Thus, in connection with the questions presented on the application for a writ of certiorari, the Class A debentures are analagous to First Preferred Stock, the Common Stock resembles Voting Second Preferred Stock and the Class B debentures are a form of Non-Voting Common Stock." Pp. 11-12.

The case was held over to the October, 1945 term of this Court (file number 100); the Answering Brief for Respondent (GB&W) reiterated the foregoing characterization of the securities (pp. 3 and 16). Thus, the GB&W argued, the case involved the internal affairs of a Wisconsin corporation which

ought to be decided in a court of Wisconsin, not New York. This Court held that the Federal Court in New York, applying Wisconsin law under *Erie R. Co. v. Tompkins,* 304 U.S. 64 (1938) and *Klaxon Co. v. Stentor Electric Mfg. Co.,* 313 U.S. 485 (1941) should take jurisdiction and decide the case under Wisconsin law. *Williams v. Green Bay & Western R. Co.,* 326 U.S. 549 (1946). Upon remand, however, the District Court in New York dismissed the case on the grounds of *res judicata. Williams v. Green Bay & W. R. Co.,* 68 F.Supp. 509 (S.D.N.Y. 1946).

While the *Williams* case had been pending in the federal courts, another group of B debenture holders had commenced a parallel class action in the Circuit Court for Brown County, Wisconsin; the decision of the Wisconsin trial court provided the basis for the *res judicata* defense in *Williams.* The Wisconsin class action was appealed to the Supreme Court of Wisconsin which decided the case on its merits. *Biltchik v. Green Bay& W. R. Co.,* 250 Wis. 177 (1947) (App 29a). The Supreme Court of Wisconsin was directly faced with the issue of whether, as the plaintiff B debenture holders contended, the B debentures were debt instruments entitled to distribution of all annual earnings or whether, as the GB&W and its directors contended, the B debentures were really the junior *equity security* of the corporation (Non-Voting Common Stock) whose rights were subject to the discretion of the directors. The brief of the GB&W and its directors, in the record below, reiterated their position cited above in the *Williams* case. The Supreme Court of Wisconsin, after reviewing the language of the debentures and the circumstances under which they were issued, concluded:

> "This as to distribution on liquidation puts the holders of the Class B debentures on the footing of stockholders of an ordinary corporation. It makes them, instead of the stockholders, the owners of the equity of the corporation. . . . This makes the payment out of the earnings of any year discretionary with the directors; that is they may retain the net earnings of any year after the Class A debenture

holders and stockholders have been paid to apply to betterments if in their reasonable judgment proper management so requires." 250 Wis. at 181, (App. 33a).

B. Subsequent Corporate Management.

During the 30 years after the *Biltchik* decision, the directors of the GB&W, elected by the capital stockholders, exercised their discretion to (1) pay the full 5% distributions on capital stock and A debentures, (2) pay nominal fluctuating distributions on the B debentures and (3) repurchase out of earnings 7,000 shares of capital stock, 597 A debentures, and 624 B debentures, while (4) increasing the corporate equity by more than $3,000,000. The "book value" per B debenture increased from $1,285 (per *Biltchik* briefs) to $2,380 as of December 31, 1976. Petitioner and others purchased B debentures on the open market on the basis that they were purchasing non-voting common stock representing an increasing equity.

In 1974 Burlington Northern, Inc. submitted a tender offer of $100 per share of capital stock, $1,000 per A debenture, and $250 per B debenture (total value $3,387,000), which the directors supported, subject to Interstate Commerce Commission approval. As of November, 1977, the takeover of the GB&W by another corporation was a foregone conclusion; the only issues were the form, price and terms of the takeover. In November, 1977, the directors of the GB&W and members of their families owned 8,048 of the outstanding 18,000 shares of capital stock; the directors had established their control over 16,000 shares of the capital stock. *A&K Railroad Materials, Inc. v. Green Bay & W. R. Co.*, 437 F. Supp. 636 (E.D. Wis. 1977). On November 29, 1977, Itel Corporation presented an offer to the GB&W's directors to purchase the GB&W's assets for $5,800,000 net to securities holders or, in the alternative, face a tender offer of $225 per share of stock, $1,000 per Class A debenture, and $275 per B debenture (total value

$5,806,400). Had GB&W's assets been sold, the directors would have received $804,800 for their stock ($100 per share). The directors, however, refused to consider a sale of assets.

After competing tender offers by another offeror, Itel raised its offer to a total of $8,015,350, payable $330 per share of capital stock, $1,050 per A debenture, and $325 per B debenture, and withdrew its original contingency of I.C.C. approval. The GB&W board recommended that all securities holders accept Itel's tender offer without disclosing that as a group the directors would receive $1,851,040 more for their shares on the tender offer than they would have received on a sale of assets where the B debentures would have been paid $975 per debenture. GB&W's president, the respondent H. Weldon McGee, increased the value of his 3,899 shares by $896,770. Pursuant to the tender offer, Itel purchased 99.7% of the capital stock and 77% of the B debentures; thereafter, despite substantial profits, GB&W has not paid any dividends on any securities.

C. Proceedings Below.

The amended complaint in the District Court alleged that the defendant directors of the GB&W had breached their fiduciary duty to the holders of the B debentures by their refusal to negotiate and consummate a sale of the GB&W assets and they did so for the purpose of obtaining a premium for the sale of control. The complaint further alleged that under principles of *res judicata*, quoting the *Biltchik* decision, the B debenture holders were entitled to the same fiduciary duty as the common stockholders of an ordinary corporation. Thereafter, petitioner was certified as class representative for those B debenture holders whose interests were not represented by the directors of the GB&W.

On cross motions for summary judgment, the District Court, after reviewing once again the history of prior reorganizations resulting in the formation of the GB&W, held that the *Biltchik* case was not *res judicata*, that despite the fact that the

B debentures represented ownership of the equity after payment of the other securities, "the GB&W was not designed to pursue the interests of the Class B debenture holders" (App 20a) and that, therefore, the directors had a right to structure the transaction to provide a premium for control because the B debenture holders lacked voting rights. (App 23a). The Court of Appeals affirmed, adopting the opinion below, (App 27a), and denied rehearing (App 28a). The questions presented herein were litigated in each instance.

D. Pending Litigation.

After the complaint below had been filed, five current B debenture holders filed a separate action, *Drexler v. Green Bay & W. R. Co.*, which was assigned to a different judge of the same District Court (see Appendix 2a), alleging that after the Itel takeover the directors elected by Itel ran the GB&W for the sole benefit of Itel, both by diverting corporate earnings to Itel and by following a no-dividend policy as a squeeze-out technique. The *Drexler* case has been held in abeyance pending a decision in this case and is not presently scheduled for trial.

REASONS FOR GRANTING WRIT

A. The decision below is inconsistent with the authoritative decision of the Supreme Court of Wisconsin construing the same securities; relitigating the same issue ought to be precluded under the doctrine of res judicata.

In the *Williams* case, this Court held that the B debentures were subject to construction under Wisconsin law. In *Biltchik* (App 29a), the Supreme Court of Wisconsin reviewed the history of the B debentures and construed them as being the same as common stock of an ordinary corporation. The District Court below, affirmed by the Court of Appeals, again reviewed the same history of the B debentures and concluded that these securities were not entitled to the same protection given

noncontrolling shareholders of an ordinary corporation. The *Drexler* case, and any future litigation involving the B debentures, will no doubt be decided based upon whether the court adopts the construction of the Supreme Court of Wisconsin or that of the District Court below.

This Court has considered the *res judicata* and collateral estoppel effects of a prior judgment in several recent cases. This Court has held that under *res judicata* a final judgment on the merits of an action precludes the parties or their privies from relitigating issues, either of fact or law, that were or could have been raised in the action: these doctrines not only relieve parties of the cost and vexation of multiple lawsuits, conserve judicial resources, and, by preventing inconsistent decisions, encourage reliance on adjudication, but also promote the comity between state and federal courts that has been recognized as a bulwark of the federal system. *Allen v. McCurry*, 449 U.S. 90, 94-6 (1980). Despite the optimistic statement that "There is little to be added to the doctrine of *res judicata* ..." in *Federated Department Stores, Inc. v. Moitie*, 452 U.S. 394, 398 (1981), *res judicata* issues were again before this Court in *Underwriters National Assurance Co. v. North Carolina Life*, 455 U.S. 691 (1982) and in *Arizona v. California*, 456 U.S. 912 (1983).

The decisions below demonstrate that the principles of *res judicata* require further authoritative development. In *Biltchik*, the Supreme Court of Wisconsin, based upon the language and history of the B debentures, held that the B debentures were on the footing of stock of an ordinary corporation and represented the equity ownership of the corporation. The courts below have now held that this holding does not preclude an inconsistent holding, based on a rereading of the same facts, that the B debentures are substantially different and represent *no* cognizable interest in the GB&W.

The *Biltchik* decision clarified the status of the B debentures in accordance with the position taken by the GB&W and its directors. The Supreme Court of Wisconsin, based on the

debenture provision limiting annual and liquidating payments on the other securities, concluded that the residual equity belonged to the B debentures and was administered for their benefit by the directors, who retained the discretion either to distribute annually or retain earnings within the corporation to build up the equity owned by the B debenture holders. The discretion vested in the directors was exactly the same as that of directors of an ordinary corporation, with the only difference being that the residual equity was owned by holders of B debentures, rather than holders of common stock. The grant of discretion implies a duty to apply it in good faith, i.e., a fiduciary duty.

All parties to this litigation are in privity with the parties to the *Biltchik* case. For 30 years, B debentures were purchased and held on the basis of *Biltchik*, irrespective of the reasons why these securities were called debentures. Yet, the federal courts below have seen fit to reconstrue the debentures to reach an inconsistent conclusion. The *Biltchik* decision contains no indication that the discretion granted to the directors was any different from that discretion normally limited by the fiduciary duty of directors to shareholders lacking corporate control.

This Court should review this case to clarify at least two points regarding application of the principles of *res judicata*: (1) a prior decision construing the relationship between those in privity with present litigants is not subject to the "distinction" that the same issue was decided in the context of a different facet of the same relationship; and (2) where a state Supreme Court has defined a relationship in terms of a common legal relationship, federal courts may not disregard the conclusion on the grounds that it is "merely an analogy," (App 18a) rather than a definition. The federal courts below have failed to give the proper preclusive effect to the decision of the Supreme Court of Wisconsin and the other courts which have construed the B debentures, through failure to apply *res judicata* principles which ought to be, but have not been, authoritatively decided by this Court.

B. The decision below raises significant issues regarding the duty of corporate directors, in a takeover situation, to protect the interests of nonvoting equity securities holders.

The decision below concluded that because B debentures lack power to vote for directors, corporate directors have no fiduciary duty to protect the interests of the holders thereof when considering the form of a corporate takeover. Thus, the District Court concluded, corporate control can be used to obtain a premium for the sale of such corporate control.

In 1968, Congress enacted the Williams Act, 15 U.S.C. §§ 78m (d)-(e) and 78n (d)-(f) 82 Stat. 457 for the purpose of providing protection to public equity investors during the course of corporate tender offers by requiring, *inter alia,* equal tenders for all securities of the same class. *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977). In so doing, Congress preempted state legislation controlling cash tender offers. *Edgar v. Mite Corp.*, 451 U.S. 968 (1982). The provisions of the Williams Act, however, provide no protection to non-voting equity investors, such as the GB&W's B debenture holders, in situations such as occurred in the case at bar where directors have manipulated the corporate affairs and thereby forced the mode of the corporate takeover into a tender offer for the purpose of discriminating against that class.

This Court has further held that equity investors are not protected from a manipulation of corporate affairs under § 10 of the Securities Exchange Act of 1934, 15 U.S.C., § 78(j). In *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462 (1977), this Court held that an investor seeking relief from a merger designed to squeeze out his interest for an inadequate consideration had a remedy under state law appraisal statutes. However, appraisal statutes are inapplicable where the transaction involves a sale of corporate securities rather than a corporate transaction. Hence, despite the comprehensive

protection intended to be provided to investors under the federal securities laws, those laws provide no remedy to a class of investors whose interest is not protected by the directors in their control of corporate affairs. That protection has traditionally been provided through imposition of a fiduciary duty.

In the case at bar, all parties agreed that a takeover of the GB&W for a total price of $8,000,000 net to securities holders was in the best interests of all parties. Had the directors sold the assets for that price, capital stockholders would have received the maximum of $1,800,000 ($100) per share and the B debenture holders $6,200,000 or $975 per debenture. The raise in offers from Itel's initial $5,800,000 offer ($625 per B debenture) to $8,000,000 should have benefited the B debenture holders exclusively. Yet, because the GB&W's directors refused to consider a sale of assets, the tender offer effectively created a premium for control to the extent of $230 per capital share in order to acquire the GB&W. Of this premium, 44% went directly into the pockets of the directors, who owned 44% (8,048 out of 18,000 shares outstanding) of the capital shares. In the case at bar, it is uncontroverted in the record that the directors refused to sell the GB&W's assets and thereby encouraged a tender offer in order to increase the return to the capital stockholders above the liquidating value of $100 per share.

The *Biltchik* decision, *supra,* was based on the premise that the corporate assets were equitably owned by the B debenture holders who, like stockholders of an ordinary corporation, would derive the principal benefit from proper corporate management upon a sale, reorganization or liquidation of the corporation. Once the GB&W's assets were saleable for an amount satisfactory to the only securities holders having an interest in the sales price, B debenture holders, the directors abused their control by refusing even to attempt to sell.

The courts below have erred in concluding that the GB&W's directors had the right to select which intracorporate group would have its interests represented. Significantly, the courts below cited no authority for that proposition, which is contrary to this Court's authoritative statement that the

> "standard of fiduciary obligation is designed for the protection of the entire community of interests in the corporation creditors as well as stockholders." *Pepper v. Litton*, 308 U.S. 295, 307.

The courts below have not decided this case based on any peculiar vagaries of Wisconsin law relating to fiduciary duties. The 7th Circuit has previously cited with approval a decision of the same District Court holding that Wisconsin law, under some circumstances, imposes a fiduciary duty upon corporate directors toward creditors. *Burroughs v. Fields*, 546 F.2d 15 (7th Cir. 1976), citing with approval *Malloy v. Korf*, 352 F. Supp. 569 (E.D. Wis. 1972). Rather, the courts below have purported to establish a general principle of corporate law which enables directors to manipulate corporate affairs without regard to the corporate interests of non-voting equity securities holders such as the holders of B debentures in the GB&W.

If, as the courts below have held, directors may disregard the interests of non-voting securities holders, then those investors have no protection in a takeover situation either under corporate law or under the broad range of protections granted under the federal securities laws. The decision below has deprived holders of non-voting securities of any remedy for the protection of their investments. The justification in the *Biltchik* decision, that corporate distributions may be withheld because the accumulated earnings will ultimately inure to the benefit of holders of B debentures is entirely illusory if directors have no obligation to protect those interests. The abuses of control to obtain undue advantages which were disapproved by the

federal courts in the leading cases of *Perlman v. Feldmann*, 219 F.2d 173 (2nd Cir. 1955), *cert. denied* 349 U.S. 952, and *Zahn v. Transamerica Corp.*, 162 F.2d 36 (3rd Cir. 1947) are now acceptable if, as below, they are inapplicable to protect the interests of non-voting securities.

This Court should review this case to clarify that general principles of corporate law, in conjunction with the protection granted investors under the federal securities laws, require that corporate directors must consider corporate takeovers consistent with their duty to protect the entire community of corporate interests, whether voting or non-voting, in a takeover situation. If non-voting investors are not entitled to have their rights protected by directors, they will be deprived of any remedy where a corporate takeover is structured to deny them the benefits of their investment.

CONCLUSION

For all of the foregoing reasons, a Writ of Certiorari should issue to review the Order of the Court of Appeals for the Seventh Circuit affirming and adopting without comment or decision the opinion of the United States District Court for the Eastern District of Wisconsin; this case should be remanded with directions that the Courts below grant Petitioner and the class he represents relief consistent with that of common stockholders in an ordinary corporation whose interests have been violated by the directors' breach of fiduciary duty to them.

Respectfully submitted,

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APPENDIX

United States District Court

EASTERN DISTRICT OF WISCONSIN

AXEL N. ELIASEN, on behalf of himself and all others similarly situated, *Plaintiff*, v. GREEN BAY & WESTERN RAILROAD COMPANY, H. WELDON McGEE, R. B. WILSON, JOHN WINTHROP, and CHARLES W. COX II, *Defendants*.	Civil Action No. 80-C-1092

DECISION AND ORDER

The plaintiff in this action, Axel N. Eliasen, sues as the representative of a class consisting of all holders of Class B debentures of the defendant Green Bay & Western Railroad Company (GB&W) as of November 29, 1977, excluding the members of the board of directors and those persons and entities holding such debentures for the benefit of the directors or members of their families. The individual defendants, H. Weldon McGee, R. B. Wilson, John Winthrop, and Charles W. Cox II, were directors of the GB & W in November of 1977. The plaintiff alleges that the individual defendants breached their fiduciary duty to the holders of Class B debentures by failing to act on an acquisition proposed by Itel Corporation (Itel) in a letter dated November 26, 1977, and by subsequently recommending acceptance of an Itel tender offer. The plaintiff further alleges that Itel's subsequent acquisition of the GB&W through a tender offer was a *de facto* sale or reorganiza-

tion of the railroad which entitles the holders of the Class B debentures to a *pro rata* distribution of the net proceeds after payment to persons with prior claims. The plaintiff seeks damages and liquidation of the GB&W, if necessary, to satisfy the claims.

On August 3-4, 1982, this case came before the Court for oral argument. The argument was primarily held to assist the Court's consideration of the pending cross-motions for summary judgment. Plaintiff filed a motion for interlocutory summary judgment on the issue of liability on September 21, 1981. This was followed by the defendants' motion for summary judgment filed on October 19, 1981. For the reasons given below, defendants' motion will be granted and the plaintiff's motion denied.

Other motions presently before the Court are the defendants' motion to strike Robert K. Steuer's affidavit submitted in support of plaintiff's motion for summary judgment, defendants' motion to consolidate this action with the case of *Drexler v. Green Bay & Western Railroad*, No. 80-C-1155 (E.D. Wis., filed Dec. 23, 1980), currently before Judge Warren, and the defendants' motion to file second amended answers. The defendants' motion to add a counterclaim, filed on January 27, 1982, was withdrawn by the defendants at the oral argument. This Court's disposition of the summary judgment motions renders these remaining motions moot.

The plaintiff Axel N. Eliason is a citizen of the State of Illinois. The defendant GB&W is a railroad corporation organized and existing under the laws of the State of Wisconsin with its principal offices in Green Bay, Wisconsin. The individual defendants are all citizens of states other than Illinois. Therefore, this court has diversity jurisdiction under 28 U.S.C. § 1332.

1. ***Facts Giving Rise to This Suit***

The GB&W was created in 1896 by taking over the assets of a railroad then in foreclosure and receiving $600,000 in newly contributed capital. The capital structure after reorganization was as follows:

Capital stock, $2,500,000, $100 par value.

Class A debentures, $600,000, $1,000 face value.

Class B debentures, $7,000,000, $1,000 face value.

Pursuant to the plan of reorganization, the 25,000 shares of capital stock were issued to the holders of the first mortgage bonds of the predecessor company, the 600 Class A debentures were issued to the contributors of the $600,000 seed capital, and the 7,000 Class B debentures were issued to the holders of the second mortgage bonds and the common and preferred stock of the old company. None of the three classes of securities had maturity dates or fixed rates of return. Annual payments on all classes were subject to the discretion of the board of directors, up to a maximum of five percent on the capital stock and Class A debentures. Only the capital stock had voting rights.

This capital structure remains intact today. The Class B debentures were reissued in 1957, but the material provisions on the debentures remained the same. Over the years, however, the GB&W purchased some of its securities so as to reduce the number of outstanding securities. By 1975, the following securities were outstanding:

Capital stock, 18,000 shares.

Class A debentures, 3 debentures.

Class B debentures, 6,376 debentures.

The plaintiff's claim for relief is based upon a series of events beginning in late 1974 and finally culminating in the acquisition of a majority stock interest in the GB&W by Itel Corporation. On October 22, 1974, the Burlington Northern,

Inc. (BN), made a public tender offer for all classes of GB&W securities. The terms of the offer, subject to Interstate Commerce Commission (ICC) approval, were $100 per share for common stock, $1,000 for each Class A debenture, and $250 for each Class B debenture. The GB&W board of directors voted to support the BN offer.

During the pendency of the BN offer, a consortium of competing midwestern railroads opposed the BN offer before the ICC and the courts. These railroads were the so-called "Three Lines"—the Soo Line Railroad Company; the Chicago, Milwaukee, St. Paul & Pacific Railroad Company; and the Chicago & Northwestern Transportation Company. Also opposing the BN offer before the ICC were a group of Class B debenture holders, led by Joseph M. Drexler, who complained that they were not offered enough for their securities. The plaintiff in this action, Mr. Eliasen, also wrote letters to the ICC, generally opposing the BN offer, supporting the application of the Three Lines to purchase and liquidate GB&W's railroad and property, and endorsing the position of Mr. Drexler. On July 15, 1977, the ICC issued a report approving the BN offer, rejecting the Three Lines' opposition thereto and applications to purchase the assets, and expressly rejecting the objection raised by Mr. Drexler on the grounds that if the Class B debenture holders did not like the price offered by BN, they had only to hold on to their securities to protect their rights fully. The Three Lines then obtained a stay of the ICC approval from the Seventh Circuit Court of Appeals.

While the ICC approval of the BN tender offer was thus stayed, a new tender offer was made by the Brae Corporation. Mr. William Texido, a former officer of Itel, formed the Brae Corporation (Brae) on August 7, 1977, to engage in the business of leasing railroad freight cars. On November 22, 1977, Brae made a tender offer for all classes of GB&W securities, offering $150 per share of common stock, $1,000 per Class A debenture, and $275 per Class B debenture.

This offer was outstanding when on November 28, 1977, Mr. Weldon McGee, the president of GB&W, received a telephone call from Mr. Joseph Costello, the president of Itel's SSI Rail Corporation (later to become Itel Rail Division). During this call, Mr. Costello informed Mr. McGee that Itel had mailed a letter dated November 26, 1977, expressing Itel's interest in acquiring the GB&W. Mr. McGee responded that he had not received the letter and that he was leaving for New York that day to attend a meeting of the GB&W board of directors on the following day. The primary purpose of that meeting was to consider the Brae offer.

Thus, Mr. Costello had a copy of Itel's letter of November 26, 1977, delivered by messenger to the GB&W board of directors meeting in New York on Tuesday, November 29, 1977. The letter expressed Itel's interest in effecting a statutory merger or purchase of assets of GB&W for $5,800,000. Itel's letter also stated that if the board did not respond favorably to the suggested merger or sale of assets, Itel would make a tender offer for GB&W securities of $225 per share of stock, $1,000 per Class A debenture, and $275 per Class B debenture.

The board received and considered the Itel proposal but did not act upon it because the Itel acquisition required ICC approval, which presumably would result in the same delays that were still holding up the BN offer. Instead, the board voted to recommend the Brae offer to the securities holders. The Brae offer had already lured most securities out of the BN escrow, and the BN had indicated that it would not issue an amended tender offer. Thus, although the ICC finally approved the BN offer on November 30, 1977, the day after the board meeting, the BN withdrew its tender offer on December 1, 1977.

During the November 29 meeting, Mr. McGee was called out to speak with Mr. Costello on the telephone. Mr. Costello asked what action the board had taken and, upon being told, said that he would visit Mr. McGee in Green Bay within the

next several days. Mr. McGee returned to his office in Green Bay on November 30, 1977, and received the promised visit on either Thursday, December 1, or Friday, December 2, 1977. Mr. Costello, accompanied by Itel's Detroit rail representative, Mr. Manasco, spent about a half hour between planes discussing Itel's plans with Mr. McGee.

Mr. McGee was informed that Itel had decided to make a tender offer to GB&W's securities holders. Mr. McGee implored Mr. Costello to dissuade Itel from doing so, explaining that the board had already recommended the Brae offer and that Itel would encounter protracted proceedings and obstacles in the ICC. Mr. Costello was unmoved and told Mr. McGee that the decision was irrevocable.

The next contact GB&W had with Itel was a phone call from the chief in-house counsel of Itel, Mr. Herman Howerton, who called Mr. McGee at home on an evening or during the weekend of December 3-4, 1977. This call occurred shortly after the Costello-Manasco visit to GB&W. Mr. Howerton sought an appointment at 1:30 p.m. on Thursday, December 8, 1977, to present a formal tender offer on behalf of Itel to GB&W for mailing to GB&W securities holders. The appointment was set.

Without forewarning, Brae delivered an amended tender offer to GB&W for mailing on Wesnesday, December 7, 1977. This amended offer sharply increased the prices offered for all classes of GB&W securites over the pending Brae tender offer by offering $225 per share of common stock, $1,050 per Class A debenture, and $300 per Class B debenture. After GB&W provided mailing address labels for all known securities holders, on December 7, 1977, the amended Brae tender offer was delivered to the escrow bank for mailing along with a letter signed by Mr. McGee recommending Brae's amended tender offer.

The following day, Mr. Howerton, accompanied by a Mr. Platt, appeared for his appointment. They delivered Itel's formal printed tender offer for mailing. Mr. Howerton at that time explained to Mr. McGee that Itel was presenting a voting trust plan to the ICC which would allow Itel to proceed with the tender offer by having all securities tendered paid for in cash and held in trust pending final ICC approval. Hence, even if the ICC were to deny approval of the Itel acquisition, the GB&W securities holders would already have been paid, and Itel alone would bear the risk of divesting the securities held by the trustee.

The terms of the Itel tender offer were identical to the amended Brae offer. After Mr. McGee so informed the Itel representatives, they asked Mr. McGee to inquire whether the Brae offer had been mailed. Mr. McGee telephoned the Brae escrow bank and reached Mr. Texido who refused to disclose whether the offer had been mailed. The Itel representatives then retired to a private office with a telephone, and in approximately a half hour rejoined Mr. McGee and Mr. Frederick Trowbridge, GB&W's attorney. The Itel representatives presented Mr. McGee with a handwritten letter which incorporated all the terms of the formal Itel tender offer but increased the prices offered for each class of GB&W securities. The increased prices offered by Itel were $330 per share of common stock, $1,050 per Class A debenture, and $325 per Class B debenture.

On the following day, Friday, December 9, 1977, a printed copy of the amended Itel tender offer arrived at GB&W and was mailed out with a cover letter signed by Mr. McGee. Mr. McGee's letter informed the securities holders that the board of directors of GB&W had withdrawn their recommendation of the Brae offer and were making no recommendations. On Monday, December 12, 1977, inquiries from GB&W securities holders began flowing in to GB&W and its directors seeking advice on how to proceed. The directors realized that some

board position was necessary. On Wednesday, December 14, 1977, the board sent a mailgram to all known GB&W securities holders recommending acceptance of the Itel amended offer.

On January 20, 1978, the ICC denied a Brae request for a cease and desist order that would have prohibited Itel from proceeding with the acquisition of GB&W securities by the voting trust. On October 12, 1978, the ICC finally approved Itel's takeover of GB&W, and Itel took the tendered securities from the voting trust. Itel acquired over 97% of the outstanding common stock, over 4,919 Class B debentures, and two of the three outstanding Class A debentures.

II. *History of the Class B Debentures*

A. *Facts Surrounding the Creation of the Debentures*

The Class B debentures are an unusual security that cannot easily be classified. The rights that the holders of Class B debentures enjoy cannot be ascertained merely by referring to the terms of the instrument and the GB&W's articles of incorporation. Interpretation of their rights requires an understanding of the circumstances surrounding the organization of the GB&W in 1896 and of the litigation that has already occurred over these debentures.

The railroad that was taken over by the GB&W in 1896 was constructed during the years 1871-1873 by the Green Bay & Lake Pepin Railway Company. That company had been chartered on April 12, 1866, and had raised the funds to construct the railroad. In September of 1873, the company changed its name to the Green Bay & Minnesota Rail Road Company.

On January 23, 1878, the Green Bay & Minnesota Rail Road Company went into receivership, and the mortgage bondholders foreclosed on their mortgages. On May 16, 1881, a committee of the mortgage bondholders chartered the Green Bay, Winona & St. Paul Railway Company. The property of

the Green Bay & Minnesota Rail Road Company was sold at a foreclosure sale to the Green Bay, Winona & St. Paul Railroad Company.

The new company was no more successful than its predecessor. The Green Bay, Winona & St. Paul Railroad Company defaulted on the interest payments due on its first mortgage bonds on August 1, 1888, and went into receivership on July 31, 1890. In 1892, a voluntary reorganization agreement was reached, but this reorganization did not succeed. On December 27, 1895, another foreclosure sale was ordered. At the sale in May of 1896, Mark T. Cox of Morristown, New Jersey, for a committee for the first consolidated mortgage bondholders consisting of himself, C. Ledyard Blair of New York City, and William Jay Hunt of Jersey City, purchased the property of the LaCrosse Branch of the railroad for $20,000, of which $10,000 was deposited in cash, and the property of the Main Line of the railroad for $1,000,000, of which $85,000 was deposited in cash.

On May 27, 1896, the charter of the Green Bay & Western Railroad Company was issued, embodying a plan of reorganization between the securities holders of the old Green Bay, Winona & St. Paul Railroad Company. The members of the first consolidated mortgage bond committee, Messrs. Cox, Blair, and Hunt, along with Messrs. Palmer and Wilson were identified as the purchasers of the railroad and property and as the incorporators and first board of directors of the GB&W. The articles of incorporation provided for three types of securities: $2,500,000 of $100 par value capital stock; $600,000 of $1,000 face value Class A debentures; and $7,000,000 of $1,000 face value Class B debentures.

The 25,000 shares of capital stock were distributed to the first mortgage and first consolidated mortgage bondholders of the Green Bay, Winona & St. Paul Railroad Company. The 7,000 Class B debentures were to be distributed to the holders of the second mortgage income bonds and to the holders of the common and preferred stock of the Green Bay, Winona & St.

Paul Railroad Company. However, the issuance of the Class B debentures was conditioned upon the purchase by the committee of second mortgage income bonds and preferred and common stockholders of the Green Bay, Winona & St. Paul Railroad Company of the 600 Class A debentures for the sum of $570,000 in cash.

None of the three classes of securities have a fixed rate of return, and such payments as might have been paid are not cumulative. Furthermore, none of the securities have a maturity date; the Class A and Class B debentures are payable only in the event of a sale or reorganization of the railroad and property of the company. Only the capital stock has voting power.

By its terms, the Class B debenture is subordinate to the capital stock and Class A debentures for distribution of income. The debenture provides that such income as was to be distributed would be distributed as follows:

> "[T]he holders of this series of Debentures shall in lieu of interest thereon participate in the distribution of annual net income to the following extent only; viz., so much of the annual net earnings of the said Company in any year as would be applicable to the payment of dividends on stock shall be applied as follows: viz., to the holders of Class A Debentures 2½% upon the face value thereof, or if such annual net earnings are insufficient for the payment of the same, then all of such net earnings shall be distributed pro rata among the holders of said Class A Debentures. After the payment of 2½% upon the face value of Class A Debentures, the stockholders of the Company are entitled to receive the balance of such net earnings until 2½% shall have been paid out of the same upon the par value of the said stock, and all surplus net earnings then remaining shall be paid to the holders of Class A Debentures and of the stock, pro rata, until 5% shall have been paid upon the face value of said Debentures and upon the par of said stock for such year, and any surplus net earnings arising in such year which may then remain shall be paid to and distributed among the holders of Class B Debentures pro rata."

In the event of a "sale or reorganization of the railroad and property of said company," the net proceeds would be applied first to the payment of all liens and charges. If any money were left of the proceeds after payment of all liens and charges on the property, such monies were to be distributed to the holders of Class A debentures and common stock *pro rata*. If any monies remained after payment of $600,000 to the holders of Class A debentures and $2,500,000 to the stockholders, the remainder was to be applied *pro rata* to the payment of the Class B debentures.

B. *Litigation Over the Debentures*

The GB&W prospered through the years, and the peculiar capital structure of the company spawned litigation. The first litigation involving the nature of the Class B debentures was *Green Bay & Western Railroad v. C.I.R.*, 147 F.2d 585 (7th Cir. 1945). The question before the Court was whether amounts paid to the holders of Class A and Class B debentures by the GN&W should be treated as interest or dividends under the income tax laws.

The Court held that they should be treated as dividends and justified its conclusion by reference to the character of the debentures.

> "The debentures on their face disclose that they had no fixed maturity; that the dividends were not cumulative and were payable within the discretion of the board of directors; that there was no provision for interest on unpaid dividends; that the debenture holders had no right to maintain an action in case of default as to the payment of dividends inasmuch as such payment was in the discretion of the board of directors; that the status of the debenture holders of class A was on a par with that of stockholders; and that rights of the debenture holders, both class A and class B, were inferior to those of creditors. Moreover, the investments in the debentures represent value paid in at the time of petitioner's incorporation and constitute a large part of its operating capital. Furthermore, the investments can be withdrawn only at the dissolution of the corpo-

> ration. They are subject to the hazards of the business and in our opinion may properly be designated as a part of the capital structure." 147 F.2d at 586-87.

Despite the expansive language quoted above, the holding of the Court, being a determination of the character of payments for purposes of the income tax laws, was quite narrow.

The years 1945 and 1946 witnessed efforts by the holders of Class B debentures to compel the GB&W to make annual payments of net income when net earnings were sufficient. A group of Class B debentureholders filed a class action in the United States District Court for the Southern District of New York seeking to recover what they claimed was their share of the net earnings for the years 1924 to 1943. The district court dismissed the suit on *forum non conveniens* grounds without prejudice to renewing the suit in Wisconsin.

The Second Circuit affirmed and in doing so held that the Class B debentureholders were only entitled to payments as declared by the directors. *Williams v. Green Bay & Western Railroad*, 147 F.2d 777, 779 (2d Cir. 1945), *rev'd* 326 U.S. 549 (1946). On *certiorari*, the Supreme Court held that the dismissal on *forum non conveniens* grounds was improper and reversed and remanded for trial. Before the case could be tried on remand before the district court in New York, however, a judgment was handed down in a similar suit filed by Class B debentureholders in the Wisconsin courts. The New York court held that the judgment of the Wisconsin trial court was *res judicata*. *Williams v. Green Bay & Western Railroad*, 68 F.Supp. 509 (S.D. N.Y. 1946).

The Wisconsin suit reached the Wisconsin Supreme Court. In *Biltchik v. Green Bay & Western Railroad*, 250 Wis. 177, *cert. denied* 332 U.S. 835 (1947), the plaintiffs, for themselves and all holders of Class B debentures, also sought to compel the GB&W to make annual payments of net income. The Court held that income on the Class B debentures was payable at the discretion of the board of directors and that the directors had not abused their discretion.

The holding in *Biltchik* was influenced both by the circumstances surrounding the creation of the Class B debentures and by the terms of the instrument. Regarding the 1896 reorganization, the Court found the following:

> "* * * It is clear from the undisputed evidence that had the foreclosure suit proceeded in the common course of practice to sale of the mortgaged property neither the holders of the second-mortgage bonds nor the stockholders of the old company would have received anything. The scheme of reorganization was manifestly planned to assure that the holders of the subordinate securities should receive nothing whatever until the holders of the new Class A debentures and the new stock were compensated both through current income and on liquidation of the new corporation * * *. * * *"

The very limited rights granted by the terms of the Class B debentures can only be understood by recognizing that these debentures were issued in exchange for worthless securities in the Green Bay, Winona & St. Paul Railroad Company.

The *Biltchik* Court relied on the provisions of the Class B debentures regarding the distribution of annual income and the distribution upon a sale or reorganization of the railroad. The Court said of the provision regarding distribution on sale or reorganization:

> "* * * This as to distribution on liquidation puts the holders of the Class B debentures on the footing of stockholders of an ordinary corporation. It makes them, instead of the stockholders, the owners of the equity of the corporation. * * *" 250 Wis. at 181.

In light of those provisions of the debenture, the Court held that the following provision made payment out of annual earnings discretionary with the directors: " 'the amounts, if any, payable upon this series of debentures out of the net earnings in any year, will be fixed and declared by the board of directors on or before the first day of February in the following year.' " 250 Wis. at 181. The Court held that the directors could retain

any net earnings to apply to betterments "if in their reasonable judgment proper management so requires." 250 Wis. at 181. The Court reasoned that such betterments would accrue to the advantage of the corporation and thereby to the advantage of the Class B debentureholders on sale or distribution.

III. *Tender Offer As "Sale or Reorganization"*

To determine whether the plaintiffs in this case are entitled to any recovery, the Court must first determine whether the successful tender offer by Itel in 1977 was a "sale or reorganization of the Railroad and property" of the GB&W, which by the terms of the Class B debentures would entitle the holders to payment on the principal of the debenture. The Court holds that the tender offer was not such a "sale or reorganization" and that the holders of the Class B debentures were not entitled to payment on the principal in 1977.

The plaintiff has not seriously contended that the Itel tender offer was a "reorganization" of the railroad. The meaning of the term has not changed significantly since 1896. The defendants quote a federal circuit court decision from 1894 which adopted the following definition of "reorganization" from a work by Morawetz on Private Corporations:

> "'The term 'reorganization' is commonly applied to the formation of a new corporation by the creditors and shareholders of a corporation which is in financial difficulties, for the purpose of purchasing the company's works and other property, after the foreclosure of a mortgage or judicial sale. The result of a transaction of this kind is to form a new corporation to carry on the business of the old company upon a new basis, free of its debts and obligations, except to the extent that they had been expressly assumed.'" *Symmes v. Union Trust Co.*, 60 Fed. 830, 870 (C.C.D. Nev. 1894) (Quoting from Morawetz on Private Corporations, § 812).

A more recent definition of the term is provided in Black's Law Dictionary 1462 (4th ed. 1951):

"As applied to corporation. The carrying out, by proper agreements and legal proceedings, of a business plan for winding up the affairs of or foreclosing a mortgage or mortgages upon the property of, insolvent corporations, more frequently railroad companies. It is usually accomplished by the judicial sale of the corporate property and franchises, and the formation by the purchasers of a new corporation. The property and franchises are thereupon vested in the new corporation and its stock and bonds are divided among such of the parties interested in the old company as are parties to the reorganization plan."

Both of the above definitions of "reorganization" indicate that the corporate property is transferred to a new corporation, which implies that the securityholders in the old company no longer have an interest in the property unless they exchange their securities for securities in the new company. At a minimum, the term "reorganization" implies a change in the capital structure of the old company which results in a "new" corporation.

The Itel tender offer did not result in a change of the capital structure of the GB&W, nor were the securities in the GB&W exchanged for securities in some new company. Rather, the GB&W remained intact as the company running the railroad. The tender offer merely resulted in a change in ownership of the securities of the GB&W. Thus, the Court holds that the Itel tender offer was not a "reorganization of the Railroad and property" of the GB&W.

The meaning of the term "sale" can only be understood by reference to the context in which it is used on the Class B debentures. The debentures refer to a "sale * * * of the Railroad and property of said Company." The terms "Railroad and property" are defined in *Northern Pacific Railroad v. Walker*, 47 Fed. 681, 685 (C.C. D.N.D. 1891), *rev'd on other grounds*, 148 U.S. 391 (1893):

"* * * The property of this railroad company is not limited to its railroad. It still owns many thousands of acres of its land grant. 'Railroad property' and 'the

property of a railroad company' are not equivalent terms. The term 'railroad property' is commonly understood to mean the property which is essential to a railroad company to enable it to discharge its functions and duties as a common carrier by rail. It includes the road-bed, right of way, tracks, bridges, stations, rolling-stock, and such like property. On the other hand, lands owned and held for sale, or other disposition, for profit, and in no way connected with the use or operation of the railroad, are not railroad property in the sense mentioned, but are property of the railroad company independently of its functions and duties as a common carrier. * * *"

This indicates that the sale of the railroad and property *of the company* refers to the sale of property owned by the company.

By contrast, a tender offer, if accepted, results in the sale of ownership of the equity securities of the company; depending on the amount of equity securities tendered and sold to the purchaser, the transaction may or may not result in the purchaser getting control of the company and may or may not result in the purchaser acquiring part or all of the equity securities outstanding.

The plaintiff cites *Dunnet v. Arn*, 71 F.2d 912 (10th Cir. 1934), for the proposition that a tender offer is, in substance and effect, a sale of the assets of the company. However, this statement in *Dunnett* was made in the context of deciding whether the directors were liable to other stockholders for secret profits made on the sale of a company. Here the question is whether the "sale * * * of the Railroad and property of said Company," construed as a contractual provision contained in the Class B debenture, was intended to include sales of stock sufficient to control the company. The Court holds that this language of the Class B debenture was not intended to include tender offers, and that the 1977 tender offer by Itel was not a "sale or reorganization of the Railroad and property" of the GB&W.

IV. *Directors' Fiduciary Duties to the Class B Debentureholders*

Plaintiff's more substantial argument is that the directors of the GB&W violated their fiduciary duty owed to the Class B debentureholders. Plaintiff alleges that the directors breached their duty in two respects. First, plaintiff argues that by failing to pursue Itel's proposal for a sale of assets or statutory merger, the directors breached their duty to protect the interests of the Class B debentureholders and to "insure that the Class B Debenture holders were fully paid for their equity ownership of the GB&W." (Brief in support of plaintiff's motion for interlocutory summary judgment on the issue of liability," filed September 21, 1981, at 22 (hereinafter cited as Plaintiff's Brief). Second, plaintiff argues that by recommending the Itel tender offer, the directors obtained a premium on the sale of the capital stock held by them, and that the premium represented a payment made for control of the corporation. Plaintiff argues that this constitutes a course of self-dealing in which the directors, for their own benefit, sold a corporate asset, i.e., control of the corporation, at the expense of the Class B debentureholders. *Id.* at 27-41.

Plaintiff has approached the fiduciary duty issue by claiming that the Class B debenture is a debenture in name only, and that it actually occupies the same position as that occupied by common stock in an ordinary capital structure. Plaintiff claims that this was the holding of the Wisconsin Supreme Court in *Biltchik v. Green Bay & Western Railroad,* 250 Wis. 177, *cert. denied* 332 U.S. 835 (1947), and that *Biltchik* is *res judicata* in this action. Since the Class B debentureholders are in reality the common stockholders of the GB&W, plaintiff concludes that the directors of the GB&W owe the Class B debentureholders all of the usual fiduciary duties that directors owe to stockholders of their corporation.

Defendants similarly approach this issue by arguing that the Court should categorize the Class B debenture, except the defendants argue that the debenture should be classified as an

income bond. Defendants also claim that *Biltchik* is *res judicata* on this issue. At oral argument, defendants referred to the decision of the trial court in *Biltchik*, which stated that the Class B debentures were income bonds. The result of the trial court decision was upheld by the decision of the Wisconsin Supreme Court.

This Court rejects the categorization approach. The bundle of rights held by the Class B debentures defies easy classification of the debentures. Thus, such classification does not aid the analysis of what duties the directors owed the Class B debentureholders.

The Court also concludes that *Biltchik* is not *res judicata* for purposes of the issues posed in this case. *Biltchik* only decided what rights the Class B debentureholders have to annual income earned by the GB&W. The trial court's reference to the debentures as "income bonds" must be read in this context. Further, although the supreme court stated that "as to distribution on liquidation" the debentureholders were "on the footing of stockholders of an ordinary corporation," this statement was made as an analogy in the context of the Court's conclusion that the increased equity of the GB&W will benefit the Class B debentureholders upon payment on the bonds. The Court was not concluding that the Class B debentureholders enjoyed all the rights of common stockholders, nor that they were the only security holders with an interest in the equity of the GB&W. Rather, the Court was simply observing that by their terms, the Class B debentures are to be paid out of the equity of the company that remains after payment of prior claims and of $600,000 to the Class A debentureholders and $2,500,000 to the capital stockholders.

The better approach is to examine the particular duties that the plaintiff claims the directors owed the Class B debentureholders, and to determine whether such duties are reasonably implied by the existence of corresponding rights held by the Class B debentureholders. This approach is suggested by the following quotation that appears in Plaintiff's Brief at 17:

"* * * [T]o say that a man is a fiduciary only begins the analysis; it gives direction to further inquiry. To whom is he a fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? * * *" *SEC v. Chenery Corp.*, 318 U.S. 80, 85-86 (1943).

That the directors of the GB&W owed *some* duties to the holders of Class B debentures cannot be disputed. The question which the Court now considers is whether the obligations the directors owe the Class B debentureholders as fiduciaries include the obligations claimed by the plaintiff.

A. ***Duty to Pursue Itel's Proposal for a Sale of Assets or Statutory Merger***

The plaintiff argues that the directors owed a duty to insure that the holders of Class B debentures would be fully paid for their equity ownership in the GB&W when the GB&W was sold (this assumes that the sale of the common stock is the same as the sale of the GB&W). Since a sale of assets or statutory merger would have led to a larger payment to Class B debentureholders while the tender offers provided for a lesser payment, plaintiff concludes that the directors owed a duty to negotiate with Itel about Itel's proposal for a sale of assets or statutory merger.

Plaintiff seems to assert two bases for this duty. First, Plaintiff's Brief at 25 states:

"* * * The Board of Directors, as the managing body of the GB&W, was required to exercise business judgment and to react favorably to the Itel offer to purchase the assets of the railroad, because the provisions of both the Articles of Incorporation and the Class B Debentures contemplated that upon a transfer of control of the railroad, its property and assets, the Class B Debenture holders would be paid fully for their equitable ownership of the railroad."

This contention cannot be maintained. As explained in part III of this decision, the payment to the holders of Class B debentures was not to be made upon any transfer of control of the railroad but only upon a "sale or reorganization" of the railroad. Nothing in the articles of incorporation or the debentures required that the directors bring about a "sale or reorganization" whenever an opportunity for such arose, or that the directors prefer a "sale or reorganization" to a tender offer.

The other basis that plaintiff asserts for imposing this duty on the directors is the *Biltchik* case. Plaintiff argues that *Biltchik* found that the Class B debenture is in effect the true common stock of the GB&W. As stated above, this Court does not so read *Biltchik*. Whatever the exact interest of the Class B debentureholders in the equity of the GB&W upon a "sale or reorganization," the debentures cannot be equated to common stock.

Nonetheless, because the payment of the debentures on "sale or reorganization" is to be made from the equity of the GB&W, the defendants admitted at oral argument that the directors would owe the debentureholders a duty to properly manage the assets of the corporation so that payment could be made upon a "sale or reorganization." But the plaintiff asserts a broader duty to generally protect the interests of the Class B debentureholders, apparently in preference to the other security holders the Court cannot find such a duty.

While most corporations operate primarily to benefit those who in the end "own" the corporation, the common stockholders, the GB&W was not designed to pursue the interests of the Class B debentureholders, whatever their interest in the equity of the GB&W. The history of the 1896 reorganization indicates that the "GB&W's structure of priority and control was adapted entirely to protect the investment of the holders of the capital stock and Class A Debentures." (Plaintiff's Brief at 19.) This was the conclusion of the *Biltchik* court and is admitted by the plaintiff. For this reason, the Class B deben-

tureholders were given no control over the corporation. The bonds were offered to give some hope of eventual recovery to the stockholders and second mortgage bondholders of the Green Bay, Winona & St. Paul Railroad Company, who would have recovered nothing had that railroad been foreclosed.

Thus, the directors owed the Class B debentureholders no duty to negotiate a sale of assets or statutory merger in preference to a tender offer in which the Class B debentureholders would receive less. The tender offer presented the Class B debentureholders with the opportunity to sell their debentures at an attractive price, albeit one less than they would have received had a "sale or reorganization" taken place. By refusing to sell the debentures, the debentureholders fully retained whatever right they had to payment from the equity of the GB&W in the event of a "sale or reorganization." They have no right to complain that the directors did not act in the best interest of the Class B debentureholders because the structure of the GB&W was not designed to promote their best interests.

B. *Duty to Avoid Self-Dealing and Obtaining a Premium for Sale of Control*

The successful Itel tender offer that the directors of the GB&W recommended on December 14, 1977, offered $330 per share of capital stock. Plaintiff contends, and defendant McGee admitted in his deposition of July 27, 1981, Exhibit 20 of Douglas A. Woodard's affidavit in support of plaintiff's motion for interlocutory summary judgment, filed September 21, 1981, that the market price of the GB&W capital stock never exceeded $100. The difference, plaintiff argues, is a premium which was paid for control of the corporation and which must be distributed to the Class B debentureholders *pro rata*.

In support of its argument, the plaintiff cites a number of cases that stand for the proposition that when majority shareholders of a company or the officers or directors of the company utilize their position of control to benefit themselves at the

expense of the corporation or the minority shareholders, that benefit may be recouped by the corporation or minority shareholders. See Plaintiff's Brief at 31-39. The principle which is at stake is summarized in a quote contained in Plaintiff's Brief at 32 n. 10:

> " 'If a purchaser interested in acquiring control of a corporation's business or its assets approaches the corporation's directors and officers and offers to buy the corporation's assets or acquire it by merger or consolidation, and if the negotiations evolve into a sale by the directors and officers of a controlling block of the corporation's stock at a premium; the sellers may be required to account to the corporation for the premium or to divide it with the other shareholders on the theory that the sellers have diverted a favorable corporate opportunity to sell assets or merge or that they have unfairly frustrated corporate action which, if consummated, would have benefited all shareholders in proportion to their holdings.' F. O'Neal, *Oppression of Minority Shareholders* 194 (1975)(footnote omitted)."

Plaintiff summarizes the cases it cites by concluding that as a general rule, majority shareholders may receive a premium for the transfer of control but that this general rule does not apply when two "indicia of unfairness" are present: "first, the prospective purchaser was interested only in acquiring the assets of the target corporation; and second, the purchaser paid a premium to acquire control of the assets which was wrongfully pocketed by the majority, at the expense of the minority." (Plaintiff's Brief at 39.) Plaintiff asserts that these indicia are present in this case.

The Court cannot accept plaintiff's conclusion that any premium the capital stockholders of the GB&W received for transfer of control must be disgorged. In all the cases cited by plaintiff, recovery was sought by the minority shareholders in the corporation and the award was based on their rights as minority shareholders. The holders of the Class B debentures cannot be said to be the minority shareholders of the CB&W [sic]

Plaintiff's claim that the Class B debentureholders are actually minority shareholders of the GB&W rests on plaintiff's conclusion that *Biltchik* found the Class B debentures to be the common stock of the GB&W. The Court does not accept this reading.

However, since the Class B debentureholders have some interest in the equity of the GB&W, and since they have no right to control the corporation, plaintiff concludes they are in the position of minority shareholders. The difficulty with this argument is that the Class B debentureholders cannot claim that the capital stockholders sold control in the corporation at the expense of the Class B debentureholders when the debentureholders have absolutely no claim to the control of the corporation. In *Dunnett v. Arn*, 71 F.2d 912, 919 (10th Cir. 1934), cited by the plaintiff, the Court stated that "it was the duty of [the officers of the corporation] to arrange such sale so that all the stockholders would be afforded the opportunity to share in the proceeds of such sale proportionately according to their stock holdings." This quotation indicates that the duty imposed on majority shareholders not to obtain a premium for sale of control of the corporation is grounded on the notion that all shares are entitled to equal rights.

In this case, the Class B debentures do not have the same rights as the capital stock. The corporation was organized in such a way as to benefit the capital stockholders and the Class A debentureholders. All rights to control the corporation were vested in the capital stockholders. The Class B debentureholders cannot now object that the capital stockholders sold their shares at a price that included a payment for a right that the capital stockholders enjoy and the Class B debentureholders do not.

The importance of this distinction can be demonstrated by an examination of the two cases relied on by the plaintiff that the Court finds factually the closest to the present case. In the leading case of *Pearlman v. Feldmann*, 219 F.2d 173 (2d Cir.),

cert. denied 349 U.S. 952 (1955), plaintiffs, minority shareholders of Newport Steel Corporation, sued Feldmann, the president, board of directors chairman, and majority shareholder of the corporation, to recoup a premium Feldmann had obtained for the sale of his controlling interest in the corporation. A purchasing syndicate was interested in buying more steel from Newport than they had been able to obtain during the recent periods of tight supply. Rather than trying to use this market leverage to benefit the corporation, Feldmann sold his controlling shares to the syndicate for $20 per share when the over-the-counter price had not exceeded $12 per share.

The Court held that Feldmann, as a corporate officer and majority shareholder, had not lived up to the duty he owed to the corporation and minority shareholders as a fiduciary. The Court reasoned:

> "* * * We have here no fraud, no misuse of confidential information, no outright looting of a helpless corporation. But on the other hand, we do not find compliance with that high standard which we have just stated and which we and other courts have come to expect and demand of corporate fiduciaries. * * * The actions of defendants in siphoning off for personal gain corporate advantages to be derived from a favorable market situation do not betoken the necessary undivided loyalty owed by the fiduciary to his principal." 219 F.2d at 176.

If the holders of Class B debentures were the minority shareholders of the GB&W, *Pearlman* would be strong support for their position in this suit. However, *Pearlman* allowed recovery because the corporation was to be run to benefit all shareholders equally. The Court stated: "[s]uch personal gain *at the expense of his coventurers* seems particularly reprehensible when made by the trusted president and director of his company." 219 F.2d at 178 (emphasis added). The holders of the Class B debentures cannot be called the "coventurers" of the directors and capital stockholders because the debentureholders had no right to control the GB&W and the capital

structure of the GB&W was designed so that the corporation would operate to benefit the capital stockholders and the Class A debentureholders, not the Class B debentureholders. Thus *Pearlman* is not applicable in this case.

The second case that merits discussion is *Zahn v. Transamerica Corp.*, 162 F.2d 36 (3d Cir. 1947). The common stock of the Axton-Fisher Corporation was of two types: Class A and Class B. The Class A stock was convertible into Class B stock at the option of the holder, and was callable by the corporation at any quarterly dividend date upon 60 days' notice at $60 per share plus accrued dividends. The Class B stock initially had all voting rights, but if there were four successive defaults on the payment of dividends to another class of stock, that other class acquired equal voting rights. Because of this provision, the Class A stock had had voting rights equal to the Class B stock since 1937. The Class A stock was entitled to twice the annual dividend of the Class B stock and was entitled to receive twice as much per share as the Class B stock upon liquidation.

By March of 1943, Transamerica Corporation had become the dominant shareholder of the corporation, holding 66-2/3% of the outstanding Class A stock and 80% of the Class B stock. The principal asset of the corporation was leaf tobacco that had cost $6,361,981 but now had a market value of $20,000,000. To obtain for itself most of the gain on the value of the tobacco, Transamerica devised a scheme whereby the board of directors of Axton-Fisher, which was dominated by Transamerica representatives, would redeem the outstanding Class A stock for $80.80 per share. Shortly thereafter Transamerica caused the liquidation of the corporation. If allowed to participate in the assets of the corporation upon liquidation, the Class A stock would have been worth $240 per share. The Third Circuit held that Transamerica had violated its fiduciary duty owed to the holders of the Class A stock.

Unlike the holders of the Class B debentures of the GB&W, the Class A stockholders in Zahn were the actual common stockholders of the corporation. They were entitled to vote upon the occurrence of four successive defaults or upon conversion to Class B stock. In this sense, the corporation was run for the benefit of the Class A stockholders, and they were entitled to participate in the control of the corporation. The Class B debentureholders of the GB&W have absolutely no claim to participate in the control of the GB&W, and they still have whatever rights they had prior to the tender offer to participate in the remainder after a "sale or reorganization of the Railroad and property of said company."

Thus this Court concludes that the defendants owed the plaintiff class no duty to not obtain a premium for the sale of the capital stock of the GB&W, representing payment for control of the corporation.

THEREFORE, IT IS ORDERED that:

1. Plaintiff's motion for interlocutory summary judgment on the issue of liability is denied.

2. Defendants' motion for summary judgment is granted, and this action is dismissed.

Dated at Milwaukee, Wisconsin, this 13th day of September, 1982.

UNITED STATES DISTRICT COURT

By: JOHN W. REYNOLDS
John W. Reynolds
Chief Judge

United States Court of Appeals

FOR THE SEVENTH CIRCUIT

Chicago, Illinois 60604

(Argued February 15, 1983)

March 11, 1983

Before

Hon. **WILLIAM J. BAUER**, *Circuit Judge*
Hon. **HARLINGTON WOOD, JR.**, *Circuit Judge*
Hon. **ROBERT VAN PELT**, *Senior District Judge**

AXEL N. ELIASEN, on behalf of himself and all others similarly situated,
Plaintiffs-Appellants,

No. 82-82-2502 *vs.*

GREEN BAY & WESTERN RAILROAD COMPANY, et al.,
Defendants-Appellees.

Appeal from the United States District Court for the Eastern District of Wisconsin.

No. 80 C 1092

John W. Reynolds, Judge.

ORDER

The decision of the district court granting summary judgment in favor of defendants is affirmed, and the district court's opinion is adopted as the opinion of this court. A copy of that opinion is attached.

AFFIRMED.

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* The Honorable Robert Van Pelt, Senior District Judge of the District of Nebraska, is sitting by designation.

United States Court of Appeals

FOR THE SEVENTH CIRCUIT

Chicago, Illinois 60604

April 14, 1983

Before

Hon. **WILLIAM J. BAUER**, *Circuit Judge*

Hon. **HARLINGTON WOOD, JR.**, *Circuit Judge*

Hon. **ROBERT VAN PELT**, *Senior District Judge**

AXEL N. ELIASEN, on behalf of himself and all others similarly situated, *Plaintiffs-Appellants*,	Appeal from the United States District Court for the Eastern District of Wisconsin.
No. 82-2502 *vs.*	No. 80 C 1092
GREEN BAY & WESTERN RAILROAD COMPANY, et al., *Defendants-Appellees.*	**John W. Reynolds**, Judge.

ORDER

On consideration of the petition for rehearing and suggestion for rehearing *en banc* filed in the above-entitled cause by the Appellant, Axel N. Eliasen, no judge in active service has requested a vote thereon, and all of the judges on the original panel have voted to deny a rehearing. Accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.

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* The Honorable Robert Van Pelt, Senior District Judge of the District of Nebraska, is sitting by designation.

Biltchik and another, Appellants, vs. **Green Bay & Western Railroad Company** and others, Respondents.

February 25—April 8, 1947.

[250 Wis. 177]

Appeal from a judgment of the circuit court for Brown county: **Arold F. Murphy**, Circuit Judge, Presiding. *Affirmed.*

[178] Action by Aaron L. Biltchik and another against Green Bay & Western Railroad Company and its directors to recover on bonds of the defendant railroad. From a judgment dismissing the complaint, entered May 14, 1946, the plaintiffs appeal. The controlling facts are stated in the opinion.

For the appellants there were briefs by *Marvin L. Kohner* and *Schmitz, Wild & Gross,* all of Milwaukee, attorneys, and *Geist & Netter* and *Netter & Netter,* all of New York, N. Y., of counsel, and oral argument by *George Netter* and *William E. Netter.*

For the respondents there was a brief by *North, Bie, Welsh, Trowbridge & Wilmer* of Green Bay, attorneys, and *F. N. Trowbridge* of Green Bay, and *Cadwalader, Wickersham & Taft, Merrill M. Manning,* and *Walter Bruchhausen,* all of New York, N. Y., of counsel, and oral argument by *Mr. Bruchhausen, Mr. Manning,* and *Mr. Trowbridge.*

FOWLER, J. The instant action was tried before the Hon. HENRY GRAASS, circuit judge for Brown county, who was killed in an automobile collision before deciding it. On stipulation the case was submited for decision to the HON. AROLD F. MURPHY, judge of the Twentieth circuit, upon a transcript of the evidence introduced before Judge GRAASS and the briefs of the parties submitted to him. The nature of the action is stated by Judge MURPHY in a written decision filed by him as follows:

> "The plaintiffs, Aaron L. Biltchik and Florence W. Brill, are holders of Class B debentures of the defendant Green Bay & Western Railroad Company, and they sue as individual security holders and on behalf of all other holders of the same securities. It is a representative action, and no other holders of the same class of securities have intervened in the action. The individuals named as defendants are the directors of the defendant railroad company.
>
> "The plaintiffs demand judgment directing the defendant directors 'to fix and declare, and the railroad company to pay [179] *pro rata* to the plaintiffs and all

other holders of Class B debentures the sum of $825,856.50 plus such amount as the court may find to be due and owing for the year 1944,' the said sum being the alleged 'annual net income and annual net earnings of the railroad company, in excess of the amounts distributable to the holders of the Class A debentures and of the common stock, for the years from 1924 to 1944, both inclusive.' . . ."

"A plan of reorganization of the predecessor company, adopted in the year 1896, and, which brought into existence a new company, the defendant railroad company, followed on the heels of a foreclosure action in the federal district court of Wisconsin. The sum of $600,000, new money, was raised and the defendant railroad company took over the assets of its predecessor after the foreclosure. The capital structure after reorganization was as follows:

"Class A income debentures, $600,000.

"Common stock, $2,500,000.

"Class B debentures, $7,000,000.

"No actual cash was paid by anyone for any of the Class B debentures. . . .

"This action is brought to recover the balance due on interest to the Class B debenture holders upon a covenant contained in the debentures which in material part reads as follows:

" '. . . the holders . . . shall in lieu of interest thereon participate in the distribution of annual net income to the following extent only, viz.: So much of the annual net earnings in any year as would be applicable to the payment of dividends on stock shall be applied as follows: (five per cent upon the face value of the Class A debentures and on the par value of the common stock) and any surplus net earnings arising in such year which may then remain shall be paid to and distributed among the holders of Class B debentures *pro rata*. None of such payments shall be cumulative. The amounts, if any, payable on this series of debentures out of the net earnings in any year, will be fixed and declared by the board of directors on or

before the first day of February, in the following year, and when so declared, any amount payable hereon will be paid. . . .' "

Of the securities above mentioned the $600,000 Class A debentures were issued to the persons who advanced the new [180] money, the $2,500,000 stock to the holders of the first-mortgage bonds in foreclosure on their surrender, and the $7,000,000 Class B debentures to the holders of the second-mortgage bonds and the common and preferred stock of the old company on their surrender. It is clear from the undisputed evidence that had the foreclosure suit proceeded in the common course of practice to sale of the mortgaged property neither the holders of the second-mortgage bonds nor the stockholders of the old company would have received anything. The scheme of reorganization was manifestly planned to assure that the holders of the subordinate securities should receive nothing whatever until the holders of the new Class A debentures and the new stock were compensated both through current income and on liquidation of the new corporation, and this must be borne in mind in construing the provisions of the Class B debentures on which the suit is based. Not only the provision for payment of dividends on the Class B debentures after the five per cent on the Class A debentures and to stockholders is paid, but all other provisions of the Class B debentures must be considered in determining what income the Class B debenture holders should receive.

The provision relied on by the plaintiffs and the only one considered by them provided that the holders of the Class B debentures—

> "shall in lieu of interest thereon participate in the distribution of annual net income to the following extent only, viz.: So much of the annual net earnings in any year as would be applicable to the payment of dividends on stock shall be applied as follows: (five per cent upon the face value of the Class A debentures and on the par value of the common stock) and any surplus net earnings arising in

such year which may then remain shall be paid to and distributed among the holders of Class B debentures *pro rata*. None of such payments shall be cumulative."

Not only this provision but two other provisions of the Class B debentures must be considered. Two of these bear [181] directly on what income the Class B debenture holders are entitled to be paid. One provides that nothing shall ever be paid on the principal until sale or reorganization of the defendant corporation, and "then only out of any net proceeds . . . after payment of any liens and charges upon such railroad or property, and after payment of $600,000 to the holders of . . . [the Class A debentures] and the sum of $2,500,000 to and among the stockholders . . . [of the instant corporation]," and that "such net proceeds remaining . . . shall be distributed *pro rata* to and among the holders of . . . the Class B debentures," This as to distribution on liquidation puts the holders of the Class B debentures on the footing of stockholders of an ordinary corporation. It makes them, instead of the stockholders, the owners of the equity of the corporation. The other provides "that the amounts, if any, payable upon this series of debentures out of the net earnings in any year, will be fixed and declared by the board of directors on or before the first day of February in the following year." This makes the payment out of the earnings of any year discretionary with the directors; that is they may retain the net earnings of any year after the Class A debenture holders and stockholders have been paid to apply to betterments, if in their reasonable judgment proper management so requires.

The defendant is a railroad corporation and as such it is the duty of its directors to keep it in proper operation and to pay the expenses of such operation and of maintaining its physical property in condition requisite for such operation, and to pay dividends to its stockholders only from its net earnings after these expenses are paid except as they may be paid out of accumulated surplus. Income on the Class B debentures not

being payable until after the five per cent dividend to stockholders is paid, income on the Class B debentures cannot be paid until after these expenses are paid. This feature is further provided for, as is also the way in which income on the Class B debentures is computed and distributed, by the provision of the Class B debentures that "the amounts [of income] [182] if any, payable upon . . . [the Class B debentures] out of the net earnings in any year will be fixed and declared by the board of directors on or before the first day of February, in the following year." Upon all the terms of the Class B debentures the holders of the Class B debentures can receive no income until after all expenses of operation and maintenance have been paid and the holders of the Class A debentures and common stock have each been paid their five per cent as interest and dividends.

The trial court found upon undisputed evidence that all gross earnings of the railroad had actually been properly applied. All not paid as interest on the Class A debentures and dividends to the stockholders and as income on the Class B debentures had actually been consumed in operating expenses and devotion to maintenance of the physical properties. The court also found that the amounts applied to maintenance and betterments were proper. The improvements made had enabled the directors to pay at least something by way of income on the Class B debentures while prior to making such improvements there had been no net income to apply to them, and the value of the equity of the owners of the Class B debentures had been thereby increased over $2,000,000. The conclusion of the trial court of proper management by the directors and officers of the corporation is supported by these facts and the direct testimony of these officers.

It is true that the evidence does not disclose that annually the directors had always acted strictly in accordance with the provisions of the Class B debentures for determining on February 1st the amount of the income payable on the Class B debentures, or that the amounts of improvements had been

determined in advance of payments of interest on the Class A debentures and dividends, but as the earnings of the corporation were all in fact applied to proper purposes to the advantage, of the corporation and to the advantage of the owners of the [183] Class B debentures, no harm or prejudice resulted to the latter by reason of the time when or the defective manner, if any, in which the expenditures were authorized or the income on the Class B debentures declared.

The view that it is discretionary with the directors whether to pay the amount of net earnings remaining in any year after five per cent has been paid to Class A debenture holders and the stockholders as dividends to the Class B debenture holders, was taken by a federal court of appeals in New York and the supreme court of the United States in *Williams v. Green Bay & W. R. Co.* (2d Cir.) 147 Fed. (2d) 777, and 326 U. S. 549, 66 Sup. Ct. 284, 90 L. Ed. 311. A case was brought by holders of Class B debenture bonds of the instant company in a United States district court of New York to recover the amount of the net income of specified years after payment of five per cent to Class A debenture holders and stockholders, *pro rata* to the plaintiff. The case was dismissed by the district court, without prejudice to bringing the action in the state of Wisconsin. This judgment was affirmed by the federal circuit court of appeals. On *certiorari* to the supreme court of the United States that court reversed the judgment and remanded the case to the federal district court for trial. While the case was decided by the federal circuit court of appeals on the sole ground whether the district court should have dismissed the case the supreme court states, p. 551:

> "The Class B debentures, issued in 1896, have no maturity date. Their principal is payable 'only in the event of a sale or reorganization' of the company and 'then only out of any net proceeds' remaining after specified payments to the Class A debentures and to the stock. The covenant in the Class B debentures out of which this litigation arises is set forth below. [See *supra*, p. 180] The

circuit court of appeals was divided as to its meaning. The majority concluded that even though there were net earnings after the payments to the Class A debentures and to the stock, the directors had discretion to deter-[184]mine whether or not that sum should be paid to the Class B debentures. . . .

"We leave open the question of the proper construction of the 'net earnings' covenant in the Class B debentures. Although we assume that the majority of the court below was right in its interpretation of the covenant, we think it was improper to dismiss the case on the grounds of *forum non conveniens.*"

When the case later came up for trial in the district court, that court, October 11, 1946, 68 Fed. Supp. 509, 512, ruled that the decision of the court below here under review construing the "Class B debentures to mean that none of the income or earnings" of the defendant is payable to the holders "unless and until" the directors "in their discretion" so declare, was *res judicata* as to that court and granted judgment of dismissal.

The same position as to action of the directors to declare a dividend to Class B debenture holders being discretionary was taken in *Green Bay & W. R. Co. v. Commissioner,* 3 T. C. 372 (7th Cir.), 147 Fed. (2d) 585. These decisions, of course, do not control this court, but are perhaps of more weight as support to our decision that payment to holders of Class B debentures is discretionary than decisions of courts in other jurisdictions generally are.

By the Court.—The judgment of the circuit court is affirmed.

FRITZ, J., dissents.

United States District Court

FOR THE

EASTERN DISTRICT OF WISCONSIN

AXEL N. ELIASEN, on behalf of himself and all others similarly situated, Plaintiff, vs. GREEN BAY & WESTERN RAILROAD COMPANY, et al., Defendants.	Civil Action File No. 80-C-1092 **JUDGMENT**

This action came on for consideration before the Court, Honorable John W. Reynolds, , United States District Judge, presiding, and a decision having been duly rendered,

It is Ordered and Adjudged:

1. Plaintiff's motion for interlocutory summary judgment on the issue of liability is denied, and

2. Defendants' motion for summary judgment is granted, and this action is dismissed.

Dated at Milwaukee, Wisconsin, this 13th day of September, 1982.

SOFRON B. NEDILSKY
Clerk of Court

By: RITA FREIS
Deputy Clerk

No. 83-27

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1983

AXEL N. ELIASEN, on behalf of himself and all others similarly situated,

Petitioner,

v.

GREEN BAY & WESTERN RAILROAD COMPANY, H. WELDON McGEE, R. B. WILSON, JOHN WINTHROP and CHARLES W. COX II,

Respondents.

ON PETITION
FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

BRIEF FOR RESPONDENTS

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QUESTIONS PRESENTED

I. Is the dicta in a Wisconsin Supreme Court decision construing the language of certain Class B Debentures, and stating that language defining payment on principal . . . "as to distribution on liquidation puts the holders of the Class B Debenture on the footing of stockholders of an ordinary corporation . . . It makes them instead of the stockholders, the owners of the equity of the corporation . . ." res judicata on the issues in this case as to whether holders of Class B Debentures (1) have the rights of stockholders of the Green Bay & Western Railroad Company (hereafter "GB&W"), and (2) stand in the shoes of minority shareholders to whom the capital stockholders and the directors would owe a fiduciary duty?

II. Did GB&W's directors have a fiduciary duty to Class B Debenture holders to oppose a tender offer and strive for a sale of assets or merger of GB&W, because a sale or merger would produce a greater return to Class B Debenture holders?

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CITATIONS TO LOWER COURT DECISIONS

The decision of the Court of Appeals for the Seventh Circuit affirming the judgment of the District Court in this case is reported among decisions without published opinions at 705 F.2d 461 (7th Cir. 1983).

AUTHORITIES OF LAW INVOLVED

If the District Court erred in holding that Biltchik v. Green Bay & Western Railroad Co., 250 Wis. 177, 26 N.W.2d 633, cert. denied 332 U.S. 835, 68 S. Ct. 216, 92 L. Ed. 408 (1947), is not res judicata in this case, then the Class B Debentures for the purposes of this case are "income bonds" and not stock, so the error, if any, was harmless.

Respondent Green Bay & Western Railroad Company is a subsidiary of Itel Corporation.

28 USC 2111

On the hearing of any appeal or writ of certiorari in any case, the court shall give judgment after an examination of the record without regard to errors or defect which do not affect the substantial rights of the parties.

Rule 61, Federal Rules of Civil Procedure

No error in either the admission or the exclusion of evidence and no error or defect in any ruling or order or anything done or omitted by the court or by any of the parties is grounds for granting a new trial or for setting aside a verdict or for vacating, modifying or otherwise disturbing a judgment or order, unless refusal to take such action appears to the court inconsistent with substantial justice. The court at every stage of the proceeding must disregard any error or defect in the proceeding which does not affect the substantial rights of the parties.

STATEMENT OF THE CASE

This case was decided below on cross motions for summary judgment upon undisputed facts. At oral argument petitioner's counsel assured the Court of Appeals that petitioner does not dispute any of the

District Court's factual findings. Contentions in the petition that conflict with the facts found by the District Court (Pet. 1a-26a) should be disregarded.

This class action, together with the copending action by certain class members in the same Court entitled Drexler, et al. v. Green Bay & Western Railroad Company, et al., 80-C-1155, constitute the second assault by Class B Debenture holders to obtain GB&W's assets. Here petitioner seeks relief from the judgment that denied his claims for damages equaling the market value of nearly all of GB&W's net worth. Petitioner claims that by operation of res judicata, the decision in Biltchik v. Green Bay & W. R. Co., which dismissed the Class B Debenture holders' earlier attempt to obtain nearly all of GB&W's net worth, requires the

Court here to arrive at the opposite result.

GB&W's Class B Debenture is a species of security devised in the 19th Century to obtain foreign funds to finance railroad construction, and to aid in reorganizing insolvent railroads. Owing to enactment of federal bankruptcy and reorganization laws, income taxation, changed economic conditions and modern developments in securities financing, that species of security has become virtually extinct. It is noteworthy here that the terms of the indenture for GB&W's Class B Debentures appear only on the faces of the debentures.

As the District Court here found on the undisputed facts, "The very limited rights granted by the terms of the Class B debentures can only be understood by recognizing that these debentures were

issued in exchange for worthless securities in the Green Bay, Winona & St. Paul Railroad Company." (Pet. 13a) That is, the Class B Debenture holders contributed nothing to GB&W that could either generate income, or provide assets with which to pay the $1,000 face value promised by each debenture. The Class B Debenture holders risked nothing. In short, the Class B Debenture holders have no greater economic justification for a claim of income or principal against GB&W than would any member of the general public. Nevertheless, the terms on the face of the debentures give holders contract claims.

GB&W's capital structure occasioned no litigation during the first 48 years of GB&W's existence. Controversy began in 1944. The IRS, on the basis of the 1936 Revenue Act, reversed its 1924

ruling and disallowed GB&W's deductions of 1937 and 1939 payments to Class A and B Debenture holders. Green Bay & Western Railroad Company, et al. v. Commissioner of Internal Revenue, 3 Tax Ct. 372 (1944), aff'd 147 F.2d 585 (7th Cir. 1945).

Also in 1944, Class B Debenture holders made their first assault on GB&W. Williams and two other Class B Debenture holders brought a class action against GB&W on behalf of all Class B Debenture holders, originally in the Supreme Court, New York County, and later removed to the U.S. District Court. Williams, et al. v. Green Bay & W. R. Co., 59 F. Supp. 98 (S.D.N.Y. 1944). Williams alleged that the terms of GB&W's Class B Debentures required payment of all surplus net income to the Class B Debenture holders, after payment to Class A Debenture holders and Capital stockholders, demanding as

damages the difference between total annual surplus net income and the amount paid on Class B Debentures. Defendant's venue motion was granted, affirmed on appeal, but reversed on _certiorari_. _Williams, et al. v. Green Bay & W. R. Co._, 59 F. Supp. 98 (S.D.N.Y. 1944); 147 F.2d 777 (2nd Cir. 1945); 326 U.S. 549, 90 L. Ed. 1311 (1946).

As here, the Class B Debenture holders also filed a second, simultaneous action in 1944. Paul Sperling on behalf of the holders of Class B Debentures sued GB&W and its directors in the Supreme Court, Kings County, seeking the same relief on the same theory as Williams. _Sperling v. McGee, et al._, 49 N.Y.S.2d 477 (1944); 51 N.Y.S.2d 274 (1944); 52 N.Y.S.2d 229 (1945); _Williams, et al. v. Green Bay & W. R. Co._, 59 F. Supp. 98

(S.D.N.Y. 1944). Defendants challenged jurisdiction, but were unsuccessful.

Meanwhile, Aaron Biltchik and Florence Brill, who were also represented by Sperling's attorneys, purchased 18 Class B Debentures and sued GB&W and its directors in the Wisconsin Circuit Court for Brown County on behalf of all Class B Debenture holders demanding the same relief on the same theories as Sperling and Williams. (A.1a-11a)* The Biltchik case was tried in January of 1946, decided on April 24, 1946 (A20a-27a), and the judgment, dated May 13, 1946, dismissed the action. The Williams case was then dismissed by summary judgment on res judicata. Williams, et al. v. Green Bay & W. R. Co., 68 F. Supp. 509 (S.D.N.Y.

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*"A" refers to the appendix to this Brief, followed by page number.

1946). Sperling's case was similarly disposed of. Sperling v. McGee, et al., 73 N.Y.S.2d 406 (1947).

The trial Court in the Biltchik case, based upon the circumstances culminating in the issue of the Class B Debentures, found that,

> The reason for the unusual provisions in the Class B Debentures, therefore, becomes crystal clear. It was not only expedient, but absolutely necessary that the Class B debentures, which were income bonds, should contain drastic restrictions as to payment of income, and that they be definitely and even arbitrarily subordinated to the holders of Class A debentures and common stockholders in the new company. (A.22a-23a)

The Biltchik Court described the subject matter litigated as follows: "This action is brought to recover the balance due on interest to the Class B debenture holders upon a covenant contained in the debentures . . ." (A.24a) Finally, the Court concluded:

> That the Class B Debentures of the defendant corporation are hereby construed to mean that none of the income or earnings of the defendant corporation is payable to or distributable to the holders of such Debentures unless and until the Board of Directors of the defendant corporation, in their discretion, so declare by resolution. (A.33a)

On appeal, the Wisconsin Supreme Court found that,

> The scheme of reorganization was manifestly planned to assure that the holders of the subordinate securities should receive nothing whatever until the holders of the new Class A debentures and new stock were compensated both through current income and on liquidation of the new corporation, and this must be borne in mind in construing the provisions of the Class B debentures on which the suit is based. (Pet.32a)*

Based on that finding, the Wisconsin Supreme Court construed the language in the Class B Debentures governing payments on income as follows:

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*"Pet" followed by a page number refers to a page in the Petition for Certiorari.

> This makes the payment out of the earnings of any year discretionary with the directors; that is they may retain the net earnings of any year after the Class A debenture holders and stockholders have been paid to apply to betterments, if in their reasonable judgment proper management so requires. (Pet.33a)

and

> Upon all the terms of the Class B debentures the holders of the Class B debentures can receive no income until after all expenses of operation and maintenance have been paid and the holders of the Class A debentures and common stock have each been paid their five per cent as interest and dividends. (Pet.34a)

The Supreme Court then affirmed. Biltchik v. Green Bay & W. R. Co., 250 Wis. 177, 26 N.W.2d 633, cert. denied 332 U.S 835, 681 S. Ct. 216, 93 L. Ed. 408 (1947).

Rumors circulating in the late 1960s and early 1970s that GB&W was about to sell its assets to, or merge with a larger railroad, led Eliasen and his broker and plaintiffs in the copending Drexler case, who are represented by the

same lawyer, to buy Class B Debentures in hopes of redemption according to the terms on the debentures. They were disappointed. Instead of a merger or asset sale, a tender offer contest developed that culminated in the 1978 acquisition of 99.7% of GB&W's outstanding capital stock and 77% of the outstanding Class B Debentures by Itel Corporation.

The disappointed Class B Debenture speculators litigated in the ICC, before the Wisconsin Commissioner of Securities, and even in the Courts (A&K Railroad Material, Inc. and Drexler, et al. v. Green Bay & W. R. Co., 437 F. Supp. 636 (E.D. Wis. 1977)), trying to force up the price offered for Class B Debentures. Their strategems failed. In desperation they filed this and the copending Drexler

actions in the District Court, directly attacking Itel's tender offer take-over. However, Itel went into Chapter XI reorganization. Plaintiffs dropped Itel from their actions rather than join the other creditors in the Bankruptcy Court, leaving only GB&W and its directors for targets.

Petitioner alleges that dicta in the Wisconsin Supreme Court's Biltchik decision converted Class B Debentures into equity securities, and, by what may be described as a quantum jump, petitioner proclaims that respondents owe Class B Debenture holders the same ficuciary duties owed to minority shareholders, if there were any. (A.46a-47a) However, respondents also pleaded res judicata (A68a), contending that the above-quoted Circuit Court decision held Class B Debentures to be "income bonds," and consequently the

rights of the Class B Debentures are defined by the express terms of the debentures.

The Courts below found that the questions of the type of security the Class B Debentures are and the rights their holders might have as a consequence were neither litigated in nor decided by the Courts in the Biltchik case. (Pet.18a) The Courts below found that Biltchik only construed the terms of the Class B Debentures affecting the holders' rights to income. (Pet.18a) The District Court then concluded on its independent review of the terms of the debentures and the plan of reorganization which resulted in creation of GB&W that Class B Debenture holders are not minority shareholders (Pet.22a) and do not have the rights of shareholders. (Pet.20a) The Court of Appeals affirmed. (Pet.27a)

Thus, Eliasen, et al. are left without a claim upon which relief could be granted, and Drexler, et al. are confined to the limitations of the Biltchik decision in their demands for income. Eliasen petitions this Court for relief from that result.

ARGUMENT

I. NO GENUINE ISSUE OF LAW, FEDERAL OR STATE, PERTAINING TO RES JUDICATA IS RAISED BY THIS PETITION.

Upon their examination of the pleadings, (A.1a-19a) abstracts of the testimony, decisions, (A.20a-27a; Pet.29a-36a) findings of fact (A.28a-35a) and appellate briefs in the Biltchik case, and the Courts below found as follows:

> In Biltchik v. Green Bay & Western Railroad, 250 Wis. 177, cert. denied 332 U.S. 835 (1947), the plaintiffs, for themselves and all holders of Class B debentures, also sought to compel the GB&W to make annual payments of net income. (Pet. 12a)

. . .

> The Biltchik Court relied on the provisions of the Class B debentures regarding the distribution of annual income and the distribution upon a sale or reorganization of the railroad. (Pet. 13a)
>
> . . .
>
> In light of those provisions of the debenture, the Court held that the following provision made payment out of annual earnings discretionary with the directors: "'the amounts, if any, payable upon this series of debentures out of the net earnings in any year, will be fixed and declared by the board of directors on or before the first day of February in the following year.'" 250 Wis. at 181. . . . (Pet. 13a)

Petitioner tacitly concedes the accuracy of the lower Courts' following statement of petitioner's contentions of res judicata:

> The other basis that plaintiff asserts for imposing thi [sic] duty on the directors is the Biltchik case. Plaintiff argues that Biltchik found that the Class B debenture is in effect the true common stock of the GB&W. (Pet. 13a)

The Courts below ruled on the application of _res judicata_ to those issues, as follows:

> The Court also concludes that _Biltchik_ is not _res judicata_ for purposes of the issues posed in this case. _Biltchik_ only decided what rights the Class B debentureholders have to annual income earned by the GB&W. The trial court's reference to the debentures as "income bonds" must be read in this context. Further, although the supreme court stated that "as to distribution on liquidation" the debentureholders were "on the footing of stockholders of an ordinary corporation," this statement was made as an analogy in the context of the Court's conclusion that the increased equity of the GB&W will benefit the Class B debentureholders upon payment on the bonds. The Court was not concluding that the Class B debentureholders enjoyed all the rights of common stockholders, nor that they were the only security holders with an interest in the equity of the GB&W. Rather, the Court was simply observing that by their terms, the Class B debentures are to be paid out of the equity of the company that remains after payment of prior claims and of $600,000 to the Class A debenture holders and $2,500,000 to the capital stockholders. (Pet. 18a)

The Courts below never reached a question of law pertaining to _res judicata_. When the lower Courts found that the issue of whether Class B Debenture holders have the rights of shareholders was not and could not have been litigated in the _Biltchik_ case, and that those courts neither decided, nor in any way acted upon that issue, there remained no possibility that the law of _res judicata_ could apply here. The Courts below found that the different passages relied upon by petitioner and respondent, when read in context, were merely explanatory of the reorganization plan, and not an action or decision on any issue in this case. This Court, in _Moses Lake Homes, Inc. v. Grant County_, 365 U.S. 744, 752 (1961), refused to apply _res judicata_ for the same reason. Therefore there is no issue

of law, state or federal, presented by this petition.

II. IF THE LOWER COURTS ERRED IN FINDING THAT THE BILTCHIK CASE IS NOT RES JUDICATA, IT WAS A HARMLESS ERROR, AND NOT A PROPER SUBJECT FOR THIS COURT'S REVIEW.

Even if this Court, upon examining the entire Biltchik record were to conclude that the lower Courts erred, and that the issue of the rights of the Class B Debenture holders dehors the express provisions on the debenture was or could have been raised in Biltchik, such error would be harmless.

First, the only statement by either Court in Biltchik declaring precisely what type of security the Class B Debenture is--not merely what it is like after liquidation of GB&W--appears in the decision of the Circuit Court for Brown County. That Court stated that the Class

B Debentures "were income bonds, . . ." (A.22a) The Wisconsin Supreme Court affirmed without mentioning the Circuit Court's statement, and without identifying the security other than calling it by name. If the Circuit Court's declaration is a decision on the issue, then the Class B Debenture holders cannot have the rights of stockholders. That is the same conclusion the Courts below reached by their independent analysis.

Second, even if the Class B Debentures were held to be equity securities by Biltchik, the holders still would not be shareholders. Only the Capital stockholders are shareholders. Hence, even if Class B Debentures were also equity securities, the rights of holders would be defined by the provisions of the debentures, and they would not have the

rights of shareholders. Cf. Broad, et al. v. Rockwell Int'l Corp., 642 F.2d 929, 940, 944, 946-948 (5th Cir. 1981); Lisman v. Milwaukee, L.S.&W. Ry. Co., et al., 163 F. 472, 480 (E.D. Wis. 1908), aff'd 170 F. 1020 (7th Cir. 1909), cert. denied 214 U.S. 520, 53 L. Ed. 1065, 29 S. Ct. 700 (1909); Carson, Pirie, Scott & Co. v. Duffy-Powers, Inc., 9 F. Supp. 199, 201-202 (W.D.N.Y. 1934). Thus, res judicata would compel the same conclusion as the lower Courts reached by their independent analysis.

Petitioner's argument on page 10 that Class B Debentures have been traded for 30 years on the basis of the Biltchik decision has no factual support. The only real purchases, by real persons for real reasons of record here are those of Eliasen, and the Drexler plaintiffs in

the copending case, who bought Class B Debentures on the basis of their construction of the terms on the debentures and rumors of an impending sale of GB&W's assets to, or a merger of GB&W with a larger railroad. Eliasen had not even heard of the existence of the _Biltchik_ case until after his purchases.

In short, the most that could be achieved by granting the petition would be to remand this case with instructions to erase the independent _ratio decidendi_, substitute _res judicata_, and leave the judgment of dismissal unchanged. A clearer case of harmless error can scarcely be imagined. Thus, the petition should be denied on the grounds that review is precluded by 28 U.S.C. 2111 and Rule 61 of the Federal Rules of Civil Procedure.

III. THE <u>RES JUDICATA</u> EFFECT OF <u>BILTCHIK</u> IS A MATTER OF WISCONSIN LAW EXCLUSIVELY, AND NOT A PROPER SUBJECT FOR THIS COURT'S REVIEW.

Federal courts must apply state law to determine the preclusive effect of a state court decision. 28 U.S.C. §1738; <u>Haring v. Prosise</u>, 103 S. Ct. 2368, 2373 (1983). This Court has stated that a challenge to a lower federal court's determination of this state law issue will "rarely constitute an appropriate subject of this Court's review." <u>Haring v. Prosise</u>, 103 S. Ct. at 2373, Note 8.

This case invokes only state law, already determined by the District Court and the Court of Appeals. Under Supreme Court Rule 17, the petition should be denied.

IV. THE DUTIES OF CORPORATE DIRECTORS TO THE CORPORATION'S SECURITIES HOLDERS ARE MATTERS OF STATE LAW, NOT FEDERAL COMMON LAW.

The petitioner's contention that Congress in enacting the Williams Act left a gap in corporate law that should be filled by a body of federal common law, which this Court should create anew for this case (Pet. 11), is singularly devoid of merit even in the context of this petition. However, it is rivaled by petitioner's later representation that the lower Courts purported to establish a general principle of corporate law to enable directors ". . . to manipulate corporate affairs . . ." (Pet. 13), which assumes in the reader a comprehensive ignorance of the lower Courts' decisions.

True, the Courts below did not base their decisions on "peculiar vagaries of Wisconsin law relating to fiduciary

duties" (Pet. 13), because the Courts below found that defendants do not have the specific fiduciary duties alleged by petitioner. GB&W is neither insolvent nor in bankruptcy as were the corporations in Burroughs v. Fields, 546 F.2d 215 (7th Cir. 1976), and Malloy v. Korf, 352 F.Supp. 569 (E.D. Wis. 1972), cited by petitioner, and corporate directors have fiduciary duties to creditors only when the corporation is insolvent. McGivern v. Amasa Lumber Co., 77 Wis. 2d 241, 252 N.W.2d 371 (1977).

The duties of corporate directors to the corporation's securities holders regarding the assets and revenue of the corporation are exclusively matters of state law as this and the lower Courts held in Williams v. Green Bay & W. R. Co., 59 F. Supp. 98, 99 (S.D.N.Y. 1944),

147 F.2d 777, 779 (1945), 326 U.S. 549, 553, 90 L. Ed. 311, 314 (1945). The petitioner can scarcely have overlooked that authority, having cited and argued it eight times on pages 4, 5 and 8 of his petition.

The petitioner's request for review to clarify general principles of corporate law (Pet. 14), sounds more like a letter to a publisher suggesting new titles for his 1983-1984 catalogue of offerings than a petition involving the jurisdiction of this Court. This and the other grounds advanced by the petition are patently frivolous, evidently asserted to delay the copending action of class members Drexler et al. who are represented by the same attorney. (See Pet. 8)

This petition fits Supreme Court Rule 49.2 which provides an award of

appropriate damages when a ". . . petition for writ of certiorari is frivolous . . ." By motion submitted herewith, respondents request award of costs including actual attorneys fees as damages.

CONCLUSION

Petitioner's transparent efforts to camouflage the nature of the case, emphasize the fact that this petition fails to present any reasons for granting *certiorari* that even colorably satisfy Supreme Court Rule 17. No question of federal law is presented. Not even a question of state law is presented. The petition only offers the possibility of a harmless error of fact and an opportunity to write a textbook on corporate law. The petition should be denied, and respondents awarded their costs and actual attorney's

fees as damages pursuant to Supreme Court Rule 49.2.

August 10, 1983.

Respectfully submitted,

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APPENDIX

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AMENDED COMPLAINT

(_Biltchik_ case)

AMENDED COMPLAINT

(Title Omitted)

Plaintiffs as above set forth, by their attorney, Marvin L. Kohner, respectfully show the Court and allege:

1. That the defendant, Green Bay and Western Railroad Company, hereinafter referred to as the corporation, is and at all times hereinafter mentioned was a corporation organized and ex-
25 isting under and by virtue of the laws of the State of Wisconsin, engaged in the business of operating a railroad, and with an office located at Green Bay, Wisconsin.

2. That the defendant company at all times hereinafter mentioned, had a board of directors; and that the present board of directors is composed of five members, namely, C. Ledyard Blair, Charles W. Cox, Robert Winthrop, H. E. McGee, and Richard B. Wilson, the individual defendants named herein.

3. That the authorized capital stock of the defendant corporation consists of 25,000 shares

of common stock of the par value of $100 each for a total of $2,500,000, all of which has been outstanding since 1896.

4. That in the year 1896 the defendant corporation, for value, also issued the following debentures, all of which are still outstanding: $600,000 principal amount of Class A Debentures, consisting of 600 Debentures with a principal amount of $1,000 each, and $7,000,000 principal amount Class B Debentures, consisting of 7,000 Debentures with a principal amount of $1,000 each.

5. That Aaron L. Biltchik, one of the plaintiffs herein, is a resident of New York City,
26 N.Y., and is the owner and holder of eight (8) of said Class B Debentures of the defendant corporation of the par amount of $1,000 each, making a total of $8,000 par value; and that the plaintiff, Florence W. Brill, is the owner of ten (10) of said Class B Debentures of the par amount of $1,000 each, making a total of $10,000 par amount of her holdings, and that the said Florence W. Brill is also a resident of New York City, N.Y.

6. That each of the Class B Debentures issued by the corporation contains the covenant that until the payment of the said debentures the holders thereof "shall in lieu of interest thereon participate in the distribution of the annual income to the following extent only, viz—So much of the annual net earnings of the said Company in any year as would be applicable

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to the payment of dividends on stock shall be applied as follows, viz—To the holders of Class A Debentures 2½ per cent upon the face value thereof, or if such annual earnings are insufficient for the payment of the same, then all of such net earnings shall be distributed pro rata among holders of said Class A Debentures. After the payment of 2½ per cent upon the face value of Class A Debentures, the stockholders of the Company are entitled to receive the balance of such net earnings until 2½ per cent shall have been paid out of the same upon the par value of the said stock, and all surplus net earnings then remaining shall be paid to the holders of Class A Debentures and of the stock pro rata, until five per cent shall have been paid upon the face value of said debentures and upon the par of stock for such year, and any surplus net earnings arising in such year which may then remain shall be paid to and distributed among the holders of Class B Debentures pro rata."

27 7. That a true and correct copy of said Class B Debenture is annexed hereto, marked Exhibit A, and is made a part hereof as though pleaded.

8. That for the years 1943 and 1944 and for a number of years prior thereto, the Corporation had annual net income and annual net earnings in excess of the amounts distributable to the holders of the Class A Debentures and of the Common Stock under the provisions of the Class B Debentures.

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9. That for each of the following years the net income or net earnings of the corporation, after deducting amounts payable to the holders of the Class A Debentures and the Common Stock was:

	1897	Nothing	1918	$ 53,556.37
	1898	"	1919	18,758.19
	1899	"	1920	63,462.46
	1900	"	1921	77,648.41
	1901	"	1922	17,500.00
	1902	"	1923	17,874.00
	1903	$53,288.43	1924	42,883.57
27	1904	50,586.64	1925	39,964.16
	1905	36,913.11	1926	37,795.67
	1906	60,894.35	1927	64,592.97
	1907	49,576.73	1928	74,278.75
	1908	27,037.09	1929	80,211.65
	1909	17,910.18	1930	90,491.57
	1910	22,099.59	1931	25,482.28
	1911	42,820.43	1932	Nothing
	1912	93,233.89	1933	"
	1913	48,882.09	1934	"
	1914	56,169.09	1935	16,161.66
	1915	52,532.79	1936	87,763.66
	1916	85,973.21	1937	153,110.51
	1917	17,140.03	1938	18,017.64
		1939	$ 88,505.48	
		1940	98,497.69	
		1941	146,165.54	
		1942	149,250.05	
		1943	443,468.68	

10. That the directors of the corporation have failed, neglected and refused to fix and declare as payable, and defendant corporation has failed to pay the sums as set forth in para-

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graph "9" hereof to the B Debenture holders, except that the directors did fix and declare as payable, and the corporation did pay to the B Debenture holders the following sums for the following years:

	1897	Nothing	1923	$ 17,500.00
	1898	"	1924	35,000.00
	1899	"	1925	35,000.00
	1900	"	1926	35,000.00
	1901	"	1927	35,000.00
	1902	"	1928	70,000.00
	1903	"	1929	70,000.00
	1904	"	1930	70,000.00
	1905	"	1931	Nothing
	1906	"	1932	"
28	1907	$35,000.00	1933	"
	1908	26,250.00	1934	"
	1909	17,500.00	1935	"
	1910	35,000.00	1936	70,000.00
	1911	35,000.00	1937	105,000.00
	1912	87,500.00	1938	Nothing
	1913	43,750.00	1939	35,000.00
	1914	52,500.00	1940	35,000.00
	1915	43,750.00	1941	70,000.00
	1916	70,000.00	1942	70,000.00
	1917	8,750.00	1943	105,000.00
	1918	8,750.00		
	1919	8,750.00		
	1920	8,750.00		
	1921	35,000.00		
	1922	17,500.00		

11. That there is due and owing from the defendant corporation to plaintiffs and to all other holders of the Class B Debentures of the corporation the difference between the amounts

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set forth in paragraph "9" hereof and the amounts set forth in paragraph "10" hereof, amounting in all to $1,299,248.61 which is equivalent to $175.61 for each $1,000 Debenture; and, in addition, the amounts which they are entitled to receive out of the earnings of the corporation for the year 1944 as hereinafter alleged.

12. Upon information and belief, that the directors of defendant corporation, the individual defendants herein, have failed, neglected and refused to fix and declare the true, full, correct and proper amount payable upon the Class B Debentures out of the net earnings of the Corporation for the year 1944, but instead have fixed and declared that the amount payable on said Class B Debentures out of the net earnings for the year 1944 is only $5.00 per $1,000 Debenture, although upon information and belief, the earnings of the Corporation for said year after deducting amounts payable to the
29 holders of the Class A Debentures and Common Stock were in excess of such amount.

13. Upon information and belief, that the 7,000 Class B Debentures of the corporation are owned and held by a large number of persons, and that such Debentures are frequently bought and sold on the security markets, and that the question in this action is one of common or general interest to all owners and holders of such debentures and it would be impracticable to bring them all before the Court.

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Plaintiffs therefore, bring this action for the benefit of all holders of said Class B Debentures of the corporation.

14. That prior to the commencement of this action a holder of Class B Debentures on his behalf and on behalf of all other holders of Class B Debentures duly demanded of the defendant corporation and of the individual defendants herein a proper acounting of the net earnings of the corporation for the year 1943 and for all prior years, and also that the de-
29 fendants make a pro rata payment to the Class B Debenture holders of the full amount of such net earnings as provided in said Class B Debentures; but defendants have altogether failed, neglected and refused to comply with said demand, and any further demand upon said defendants would be futile and unavailing.

Wherefore, plaintiffs demand judgment herein as follows:

A. Directing the individual defendants herein, who are directors of the corporation, to fix and declare, and the corporation to pay, pro rata to the plaintiffs and all other holders of Class B Debentures the sum of $1,229,248.61 plus such amount as the court may find to be due and owing for the year 1944.

B. That plaintiffs be awarded such sums as the Court may deem proper for their costs, expenses, disbursements and counsel fees for their attorneys.

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C. For such other and further relief as the Court may deem equitable and proper in the premises.

30 Marvin L. Kohner,
Plaintiffs' Attorney.
(Of Counsel, omitted)

EXHIBIT A

United States of America
Green Bay and Western Railroad Company

CLASS B

DEBENTURE

The Green Bay and Western Railroad Company hereby certifies that this is one of a series of Seven thousand of its Class B Debentures in the sum of ONE THOUSAND DOLLARS each aggregating in all the sum of Seven Million Dollars, which sum of One Thousand Dollars will be payable to the bearer hereof, or if registered to the person appearing on the books
33 of the said Company as the last registered owner hereof, only in the event of a sale or reorganization of the railroad and property of said Company, and then only out of any net proceeds of such sale or reorganization which may remain after payment of any liens and charges upon such railroad or property, and after payment of Six hundred thousand Dollars to the holders of a series of debentures known as Class A, issued or to be issued by said Company, and the

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sum of Two Million, five hundred Thousand Dollars to and among the stockholders of said Company. Any such net proceeds remaining after such payments shall be distributed pro rata to and among the holders of this series of Class B. Debentures. The said Railroad Company Hereby Covenants and Agrees that no mortgage shall at any time be placed upon its railroad and other property, nor shall the same be leased or sold without the consent of the holders of seventy-five percent of the capital stock outstanding at the time of such mortgage lease or sale. The said Railroad Company Hereby Agrees that until such payment, the holders of this Series of Debentures shall in lieu of interest thereon participate in the distribution of annual net income to the following extent, viz:—So much of the annual net earnings of the said Company in any year as would be applicable to the payment of dividends on stock shall be applied as follows, viz:—To the holders of
34 Class A Debentures 2½ percent upon the face value thereof, or if such annual net earnings are insufficient for the payment of the same, then all such net earnings shall be distributed pro rata among the holders of said Class A Debentures. After the payment of 2½ percent upon the face value of Class A Debentures, the stockholders of the Company are entitled to receive the balance of such net earnings until 2½ percent shall have been paid out of the same upon the par value of said stock, and all surplus net earnings then remaining shall be paid to the

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holders of Class A Debentures and of the stock pro rata until five percent shall have been paid upon the face value of said debentures and upon the par of said stock for such year, and any surplus net earnings arising in such year which may then remain shall be paid to and distributed among the holders of Class B Debentures pro rata. None of such payments shall be cumulative. The amounts, if any, payable upon this series of debentures out of the net earnings in any year, will be fixed and declared by the Board of Directors on or before the first day of February, in the following year, and when so declared, any amount payable hereon will be paid at the office or agency of the Company in the City of New York on or before the first day of March, in such year to the holder of this debenture, upon its production at such office or agency in order that such payment may be stamped hereon; or, if registered, payment will be made by check mailed to the person appear-
35 ing on the books of this company as the registered owner hereof at the last address furnished by him to this company. This debenture shall pass by delivery unless registered on the books of the Company at its office or agency in the City of New York, and when so registered, and registry noted hereon, title thereto shall pass only by assignment executed by the last registered owner and noted on such register. This instrument shall not be valid for any purpose unless authenticated by the signature of the Farmers' Loan and Trust Company to the certificate endorsed hereon.

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In Witness Whereof the said Green Bay and Western Railroad Company has caused these presents to be duly executed under its corporate seal at the City of Green Bay this first day of July, 1896.

Green Bay and Western Railroad Company
(Seal)

By..

By: S. S. PALMER, President

35 Attest: MARK T. COX, Secretary.

AUTHENTICATION

The Farmers' Loan and Trust Co. hereby certifies that this is one of a series of 7000 Class B Debentures of $1,000 each issued by the Green Bay and Western Railroad Company as herein set forth.

The Farmers' Loan and Trust Co.

By: William H. Leupp,
Vice-President.

ANSWER OF CORPORATION

(<u>Biltchik</u> case)

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ANSWER OF CORPORATION

(Title Omitted)

The defendant, Green Bay and Western Rail-
40 road Company, hereinafter referred to as the "Railroad Company", by its attorneys, North, Bie, Duqaine, Welsh & Trowbridge, answering the amended complaint herein, shows to the Court:

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1. Admits each and every allegation set forth in paragraphs numbered "1", "2" and "3" of the amanded complaint herein.

2. Denies each and every allegation set forth in paragraph numbered "4" of the amended complaint herein except that defendant admits that the securities described in said paragraph numbered "4" were duly issued by the Railroad Company in connection with a plan of reorganization referred to in paragraph 15 hereof, and that said securities are still outstanding.

3. Denies that it has any knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph numbered "5" of the amended complaint herein.

4. Admits each and every allegation contained in paragraph numbered "6" of the amended complaint herein but respectfully refers the Court to the Class B Debentures of which the quoted material is merely a part for the exact terms, provisions and conditions of the entire instrument.

41 5. Denies each and every allegation contained in paragraph numbered "7" of the amended complaint herein.

6. Denies each and every allegation contained in paragraphs numbered "8" and "9" of the amended complaint.

7. Denies each and every allegation contained in paragraph numbered "10" of the

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amended complaint herein, except that it admits that the Directors did fix and declare as payable and the Railroad Company did pay to the holders of Class B Debentures the sums mentioned in that paragraph and for the years therein mentioned.

41 8. Denies each and every allegation contained in paragraphs numbered "11" and "12" of the amended complaint.

9. Admits each and every allegation contained in paragraph numbered "13" of the amended complaint herein.

10. Denies each and every allegation contained in paragraph numbered "14" of the amended complaint herein.

AS AND FOR A FIRST SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

11. That the cause of action alleged in the amended complaint as to the net income, net earnings of the Railroad Company and the moneys claimed by the plaintiffs for the year 1934 and all of the years prior thereto did not accrue within ten years from the time of the commencement of this action and that the said cause of action is barred by Section 330.18, subdivisions 2 and 4, of the Statutes of this State.

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AS AND FOR A SECOND SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

42 12. That the cause of action alleged in the amended complaint as to the net income, net earnings of the Railroad Company and the money claimed by the plaintiffs for the year 1924 and all of the years prior thereto did not accrue within twenty years from the time of the commencement of this action and that the said cause of action is barred by Section 330.16, subdivision 2, of the Statutes of this State.

AS AND FOR A THIRD SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

13. Upon information and belief that the plaintiffs and their predecessors in interest and in title had full knowledge of all of the matters complained of and have delayed the bringing of this action for many years and that during those years the Railroad Company has followed practices and customs pertaining to the use and distribution of its earnings which have been acquiesced in by the plaintiffs and their said predecessors and that the granting of the relief sought by the plaintiffs would be inequitable.

AS AND FOR A FOURTH SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

14. That the plaintiffs and their predecessors in interest and in title with full knowledge of

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the matters now complained of and set forth in the amended complaint, have, during the period of many years, received, acquired, accepted and retained distributions of income under the Class B Debentures, when and as declared by the Board of Directors of the Railroad Company and have ratified the action of the said Board and are now estopped from making the claims set forth in their alleged cause of action.

AS AND FOR A FIFTH SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

43 15. That at all the times mentioned in the amended complaint herein, the defendant Railroad Company has been and now is a common carrier, owning and operating lines of railroad entirely within the State of Wisconsin; that the said Class B Debentures were issued by the Railroad Company in 1896 in connection with a plan of reorganization, following foreclosure, pursuant to which the railroads, properties, rights, powers, privileges and franchises of the Green Bay, Winona & St. Paul Railway Company and the Green Bay, Stevens Point and Northern Railway Company were sold under decrees of foreclosure and sale rendered by the Circuit Court of the United States in and for the Eastern District of Wisconsin and, subsequently, as a part of said plan of reorganization, acquired by the Railroad Company in exchange for all of its securities; that in said plan of re-

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organization the Common Stock of the Railroad Company was issued to holders of senior mortgage securities of the predecessor companies and the Class B Debentures were issued to holders of junior securities without consideration except the surrender of such junior securities; that any and all annual net income otherwise available for distribution to Class B Debenture holders in any year mentioned in the amended complaint, in excess of such income as was actually so distributed in such year, was in fact and in the judgment of the Board of Directors of the Railroad Company, necessary to said Company in order to provide for the current and prospective maintenance of its engines, cars, tracks and other equipment in such condition as adequately to accommodate the public and for the safe, adequate and efficient transportation and handling of passengers and freight, as was and is required of the Railroad Company by the laws, statutes and public policy of the State of Wisconsin, and of the United States; that any portion of net income not dis-
44 tributed and retained was due solely to said necessity and to the judgment of said Directors that the said necessity existed; that under the correct construction of said Class B Debentures, said Directors were neither required nor entitled to declare, or said Railroad Company to make, any distribution to Debenture holders of net income necessary to the Railroad Company for the above-mentioned purposes; and that any contrary construction of said Debentures, the

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applicable provisions of said Debentures themselves if so construed, and any decree or relief sought by the plaintiffs herein based upon such a construction, are and would be against public policy, illegal and void.

44 Dated, Green Bay, Wisconsin, August ...., 1945.

North, Bie, Duquaine, Welsh & Trowbridge,
Attorneys for Defendant,
Green Bay & Western Railroad Company,
Suite 509, Bellin Building,
Green Bay, Wisconsin.

ANSWER OF DIRECTORS

(Title Omitted)

The defendants, C. Ledyard Blair, Charles W. Cox, Robert Winthrop, H. E. McGee and Richard B. Wilson, severally and each for himself, by his attorneys, North, Bie, Duquaine, Welsh & Trowbridge, answering the amended complaint herein, shows to the Court:

Repeats, realleges, adopts, and incorporates herein paragraphs "1" to "15", both inclusive, of the Answer of defendant herein, Green Bay & Western Railroad Company, filed herein in the office of the Clerk of the Circuit Court for Brown County, Wisconsin, on or about the ....day of August, 1945, with the same force and effect as if set forth *in extenso* and as if all admissions, allegations and denials therein made by said Green Bay & Western Railroad Com

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pany were here separately made as and by these defendants, and as if all allegations and separate defenses therein made by said Green Bay & Western Railroad Company were here separately alleged and made as and by these defendants.

Wherefore, defendants demand judgment dismissing the said amended complaint herein on the merits with costs.

North, Bie, Duquaine, Welsh & Trowbridge,
Attorneys for Defendants,
C. Ledyard Blair, Charles W. Cox, Robert Winthrop, E. H. McGee and Richard B. Wilson,
Office and Post Office Address:
Suite 509, Bellin Building,
Green Bay, Wisconsin.

DECISION

(Biltchik case)

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APPENDIX

DECISION

(Title Omitted)

This action was heard in the Brown County Circuit Court, Honorable Henry Graass presiding. The testimony was transcribed by the official reporter and briefs were submitted, but before a decision was made and filed by Judge Graass he was killed in an automobile accident on March 8, 1946. The parties, through their respective attorneys, agreed to submit the case
52 for decision upon the record, consisting of the transcribed testimony and the exhibits, upon the briefs heretofore filed before Judge Graass.

The plaintiffs, Aaron L. Biltchik and Florence W. Brill, are holders of Class B Debentures of the defendant Green Bay & Western Railroad Company, and they sue as individual security holders and on behalf of all other holders of the same securities. It is a representative action, and no other holders of the same class of securities have intervened in the action. The individuals named as defendants are the directors of the defendant railroad company.

The plaintiffs demand judgment directing the defendant directors "to fix and declare, and THE RAILROAD COMPANY to pay pro rata to the plaintiffs and all other holders of Class B Debentures the sum of $825,856.50 plus such amount as the Court may find to be due and

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owing for the year 1944," the said sum being the alleged "annual net income and annual net earnings of the railroad company, in excess of the amounts distributable to the holders of the Class A Debentures and of the common stock, for the years from 1924 to 1944, both inclusive."

Upon the trial the late Honorable Henry Graass, presiding circuit judge, held that the twenty-year statute of limitations was applicable, thereby limiting the claim to the period from
53 1924 to 1944, inclusive.

The defense of laches, and likewise estoppel, interposed by the defendant is not tenable. The lapse of time, which in itself cannot support the defense of laches, is not available unless it has worked irreparable injury to the defendant, and there is a failure to establish any injury or prejudice of the defendant by the lapse of time. At least two previous actions by holders of Class B Debentures have been instituted and maintained to a decision. The instant plaintiffs purchased their securities a comparatively short time ago, and certainly they have acted with dispatch. There can be no claim that the defendant railroad company ever changed its position in reliance upon any conduct of the plaintiffs as a class to the defendant's damage.

A plan of reorganization of the predecessor company, adopted in the year 1896, and, which brought into existence a new company, the defendant railroad company, followed on the heels

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of a foreclosure action in the Federal District Court of Wisconsin. The sum of $600,000.00, new money, was raised and the defendant railroad company took over the assets of its predecessor after the foreclosure. The capital structure after reorganization was as follows:

Class A income debentures, $600,000.00.
Common stock, $2,500,000.00.
Class B debentures, $700,000.00.

54 No actual cash was paid by anyone for any of the Class B debentures, and under the plan of reorganization the total of seven million dollars of Class B debentures were distributed as follows: About two million two hundred twenty thousand to the holders of the old second mortgage bonds, amounting to three million seven hundred eighty-one thousand, and about three million seven hundred eighty thousand to the holders of the old common and preferred stock.

The foreclosure action would have wiped out completely the holders of the old junior securities, and the reorganization resulted in the issuance to such junior security holders the Class B debentures under consideration and involved in this case. The record discloses that for fourteen years no income had been paid on the old junior securities before the foreclosure. The reason for the unusual provisions in the Class B Debentures, therefore, becomes crystal clear. It was not only expedient but absolutely necessary that the Class B debentures, which were income bonds, should contain drastic restrictions as to

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payment of income, and that they be definitely and even arbitrarily subordinated to the holders of Class A debentures and common stockholders in the new company. The precarious condition of the company required the provision that "only in the event of a sale of reorganization of the company" would the Class B debentures be paid on the principal or face amount of the debenture; and for the same understandable reason there was no maturity date in the Class B securities.

The Class B debentures bearing the face value of one thousand dollars were, with the other
55 securities of the company immediately after reorganization, listed for sale on the New York Stock Exchange. The plaintiffs in this action, Biltchik and Brill, comparatively recently purchased on the open market Class B debentures for $120.00.

Annual reports of the railroad company showing receipts and disbursements of income and the amounts paid to security holders, and the general financial condition, were filed in the offices of the Interstate Commerce Commission, Washington, D. C., The Wisconsin Public Service Commission, Madison, Wisconsin, The Securities and Exchange Commission, both in Washington and Philadelphia, and the New York Stock Exchange in New York. The plaintiffs in no manner dispute or criticize any item in any of the reports as to the financial condition as filed.

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This action is brought to recover the balance due on interest to the Class B debenture holders upon a covenant contained in the debentures
55 which in material part reads as follows:

> " * * * the holders * * * shall in lieu of interest thereon participate in the distribution of annual net income to the following extent only, viz:— So much of the annual net earnings in any year as would be applicable to the payment of dividends on stock shall be applied as follows (five per cent upon the face value of the Class Debentures and on the par value of the common stock) and any surplus net earnings arising in such year which may then remain shall be paid to and distributed among the holders of Class B Debentures pro rata. None of such payments shall be cumulative. The amounts, if any, payable on this series of Debentures out of the net earnings in any year, will be fixed and declared by the Board of Directors on or before the first day of February, in the following year, and when so declared, any amount payable hereon will be paid * * * . "

The defendant railroad company after reorganization acquired title of its predecessor to a railroad whose tangible assets were listed at a value of $10,100,000.00. The defendant company in recent years has made a considerable profit and is operating a modern, prosperous railroad with unmortgaged assets of $13,760,-000.00 and liabilities of $560,000.00, exclusive of Class A and B Debentures and common stock. Exhibit seven, which is the financial statement

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ust referred to, shows that the assets exceed all liabilities, including Debentures in capital stock, by $3,100,000.00.

The plaintiffs contend that such excess net income, by virtue of the provisions of the Class B. Debentures, must be paid to them, and that
56 the payment in essence is only a ministerial act but, by reason of the net earnings of the company, require that the same be paid to them and that the directors have no right to withhold payment nor to exercise any discretion in the matter.

The directors annually have by proper resolution authorized payments to the various classes of securities, and at various times the holders of Class B Debentures have been paid amounts representing one-half of one per cent, one per cent, and one and one-half per cent of the face of the Debenture.

The defendants maintain that the net earnings or income is not payable to Class B Debenture holders until the directors in the proper exercise of their discretion declare that it shall be paid. The directors have not declared it to be payable, and this action is brought to compel the directors to do so.

The directors have pursued a policy of using the income for betterments and improvements which, they assert, are necessary for the proper maintenance of a modern railroad in competition with other railrads of the same class, and that such policy is in the public interest.

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The testimony of the present executives of the company, which is undisputed, makes clear the position of the company with reference to net
57 earnings or excess income, and it is undoubtedly their sound judgment and policy of plowing back part of the income that has kept the defendant railroad company in a favorable competing position with other railroads. The position of the executives of the railroad company that to insure the maintenance of the present earning power there must continuously be replacement of obsolete and outmoded equipment, and that replacement costs of this more efficient equipment, in addition to depreciation, is a heavy burden which must be borne to hold its competitive position in the industry, seems sound and not subject to constructive criticism.

The specific language of the Class B Debenture has already been interpreted and, I believe, the claims of the plaintiffs herein adjudicated in *Williams vs. Green Bay & Western Railroad Company*, 147 Fed. (2d) 777, Circuit Court of Appeals, and a decision in the same case by the United States Supreme Court as of January 7, 1946, and the case of *Green Bay & Western Railroad Company vs. Commissioner of Internal Revenue*, 147 Fed. (2d) 585, Circuit Court of Appeals, Seventh District.

The Court in *New York * * * Railroad Company vs. Nickals*, 119 U. S. 296, in construing the provisions of preferred stock as to the payment of dividends upheld the theory that the payment

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of dividends was a matter vested in the discretion of the Board of Directors, and even though dividends were earned they were not payable until declared to be payable by the Board of Directors. The Nickals case, I believe, directly rules and settles the issues in the instant case.
58 There is no claim nor showing of bad faith on the part of the Directors, and, in the absence of such showing, then the Board of Directors cannot by this type of action be compelled to pay the holders of Class B Debentures. The exercise of the discretion on the part of the Directors in withholding payment is amply justified by the application of sound business principles; and the holders of Class B Debentures must see what is obvious to anyone, that their equities in the defendant railroad company are constantly being increased and that the earnings of the company will eventually enure to their benefit.

The complaint of the plaintiffs is dismissed on its merits and defendants shall recover from the plaintiffs their actual disbursements, to be settled by the Court upon failure of agreement as to amount, and no taxable costs allowed.

Dated: April 24, 1946.

By the Court:

Arold F. Murphy,
Circuit Judge.

FINDINGS OF FACT AND
CONCLUSIONS OF LAW

(Biltchik case)

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FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Title Omitted)

At a regular term of court aforesaid begun and held in the City of Green Bay on the 16th day of January and continuing in session to this
59 date. Present, Honorable Henry Graas and Honorable Arold F. Murphy, Circuit Judges presiding.

This action coming on for trial before the court without a jury, Honorable Henry Graas, deceased, presiding, plaintiffs appearing by their attorneys, Geist & Netter and Marvin L. Kohner, defendants appearing by their attorneys, North, Bie, Dequaine, Welsh & Trowbridge and Cadwalader, Wickersham & Taft, said Judge Graas having heard the testimony, arguments of counsel and then having died, and the parties having stipulated that I, said Arold F. Murphy, do consider and decide said case, and after considering the testimony, examining the briefs and being advised on the premises, do make the following:

Findings of Fact

1. That the defendant, Green Bay and Western Railroad Company, is and at all times since June 1896 has been a corporation organized and existing under and by virtue of the laws of the State of Wisconsin, engaged in the business of operating a railroad, and with an office located at Green Bay, Wisconsin.

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2. That the said defendant since June 1896 has had a board of directors and that the present board of directors is composed of five members,
60 namely: C. Ledyard Blair, Charles W. Cox, Robert Winthrop, H. E. McGee and Richard B. Wilson, the individual defendants hereinabove named.

3. That the authorized capital stock of the defendant corporation consists of 25,000 shares of Common Stock of the par value of $100 each for a total of $2,500,000, all of which has been outstanding since 1896.

4. That since 1896 the defendant corporation has been and now is a common carrier owning and operating lines of railroad in Wisconsin and partly in Minnesota.

5. That in the year 1896 the defendant corporation issued the following Debentures, all of which are still outstanding, to-wit: $600,000 principal amount of Class A Debentures, consisting of 600 Debentures with a principal amount of $1,000 each, and $7,000.00 principal amount of Class B Debentures consisting of 7,000 Debentures with a principal amount of $1,000 each.

6. That annexed hereto are copies of the said Class A Debentures and the Class B Debentures.

7. That the said Class B Debentures were issued by the defendant corporation in 1896 in connection with a plan of reorganization, following foreclosure, pursuant to which the rail-

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road's properties, right, powers, privileges and franchises of the Green Bay, Winona & St. Paul Railway Company and the Green Bay, Stevens Point and Northern Railway Company were sold under decrees of foreclosure and sale rendered by the Circuit Court of the United States in and for the Eastern District of Wisconsin, and subsequently, as a part of said plan of reorganization, acquired by the defendant corporation for all of its securities.

8. That in the said plan of reorganization the common stock of the defendant corporation was issued to the holders of senior mortgage
61 securities of the predecessor companies and that the aforesaid Class B Debentures were issued to the holders of junior securities of said predecessor companies without consideration except the surrender of such junior securities and that the Class A Debentures were issued for cash supplied by those who received the Class A Debentures.

9. That during the years 1924 to 1944, both inclusive, the Board of Directors of the defendant corporation by resolutions fixed and declared payments on the Class B Debentures, ranging from one-half to one and one-half per; cent of their face value and at no time for a fraction of a percent less than one-half.

10. That each of the said payments when made was stamped on the reverse side of such Class B Debentures.

11. That annual reports showing the receipts, disbursements, of income of the defendant cor-

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poration and the amount paid to the security holders were filed in the offices of the Interstate Commerce Commission in Washington. The Wisconsin Public Service Commission at Madison, the Securities and Exchange Commission and the New York Stock Exchange, and that no objections to the said reports were ever made by the plaintiffs or their predecessors in interest.

12. That all of the income of the defendant corporation for the years 1924 to 1944 inclusive, other than the sums allocated and paid to the
62 security holders, was used and necessarily used in the public interest for additions and for the betterment for the defendant's railroad and to properly and adequately serve the public, to meet competition and in the best interest of the security holders.

13. That the equity of the holders of the Class B Debentures has been increased during the years 1924 to 1944 inclusive by the application of the said income to betterments and additions to the extent of more than $2,000,000.

14. That the plaintiffs are the owners of Class B Debentures of the face value of $18,000 and that they purchased them between April 7, 1943 and November 28, 1944, shortly prior to the commencement of this action, when the market value was approximately $120. per Debenture, having a face value of $1,000 and that their annual return exceeded five percent of their investment.

15. That the said Class B Debentures are owned and held by a large number of persons

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and that such Debentures are frequently bought and sold on the security markets and that the question in the action is one of common or general interest to all owners and holders of such Debentures and that it was impracticable to bring them all before this Court and that the plaintiffs brought this action for the benefit of all holders of the said Class B Debentures.

16. That prior to the commencement of this action, the plaintiffs on behalf of themselves
62 and all other holders of the said Class B Debentures duly demanded of the defendants a proper accounting of the net earnings of the defendant, corporation for the year 1943 and for all prior years and also demanded that the defendants make a pro-rata payment to the Class B Debenture holders of all of the net earnings of the defendant corporation and the defendants have refused to comply with the said demand and that any further demand is unnecessary.

17. That the plaintiffs and their predecessors in interest and in title had full knowledge or were chargeable with full knowledge of all of the matters complained of and the defendants have consistently followed a uniform custom and practice pertaining to the use and distribution of the earnings of the defendant corporation.

63 18. That the plaintiffs and their predecessors in interest and in title with full knowledge of the matters complained of and set forth in the

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amended complaint herein have, during the period of many years, received, acquired, accepted and retained distributions of income under the Class B Debentures when and as declared by the Board of Directors of the defendant and have ratified the action of the said Board.

19. That the Board of Directors have not fixed and declared the amount claimed in the amended complaint, or any part thereof, to be payable to or distributable to the holders of the Class B Debentures.

Conclusions of Law

1. That the Class B Debentures of the defendant corporation are hereby construed to
64 mean that none of the income or earnings of the defendant corporation is payable to or distributable to the holders of such Debentures unless and until the Board of Directors of the defendant corporation, in their discretion, so declare by resolution.

2. That the mere ascertainment that the said defendant corporation has income or earnings does not entitle the Class B Debenture holders thereto or any part thereof.

3. That the cause of action alleged in the amended complaint as to the net income, net earnings of the defendant corporation and the moneys claimed by the plaintiffs for the years 1924 and all of the years prior thereto did not

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accrue within twenty years from the time of the commencement of this action and that the said cause of action is barred by Section 330.161 subdivision 2, of the Statutes of this State.

4. That the Board of Directors of the defendant corporation properly and legally exer-
64 cised its discretion under the terms of the Class B Debentures in disposing of the income and earnings of the defendant corporation for the years 1924 to 1944 both inclusive.

5. That the plaintiffs and the Class B Debenture holders have no legal or valid claim against the defendants or any of them for the income or earnings of the defendant corporation or any of them.

6. That judgment shall be entered herein dismissing the amended complaint upon its merits.

7. That the original parties to the said Class B Debentures and their successors in interest and in title, including the parties to this action, at all of the times mentioned in the amended complaint have construed and enforced the said Class B Debentures by a consistent and uniform course of conduct so as to give them the meaning that the income or earnings of the defendant corporation were not and are not payable or distributable to the holders of such Class B Debentures unless and until the Board of Directors of the said corporation, in their discretion, so declared or declare by resolution.

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8. Defendants will recover from the plaintiffs their actual disbursements fixed in the sum
65 of $25.00.

Dated: May 13, 1946.

By the Court:

Arold F. Murphy,
Circuit Judge.

AMENDED COMPLAINT

(*Eliasen* case)

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WICONSIN

AXEL N. ELIASEN,
on behalf of
himself and
all others similarly
situated,

Plaintiff,

v.

AMENDED COMPLAINT

GREEN BAY & WESTERN
RAILROAD COMPANY,
H. WELDON McGEE,
A. H. SCHAEFFER,
R.B. WILSON, JOHN
WINTHROP, CHARLES W.
COX II, and ITEL
CORPORATION,

Case No. 80-C-1092

Defendants.

THE PLAINTIFF, on behalf of himself and all others similarly situated, by his attorneys, Robert K. Steuer and William J. Mantyh, states as follows:

JURISDICTIONAL ALLEGATIONS

1. The plaintiff is now and was at all times relevant hereto a citizen of the State of Illinois. The defendant Green Bay & Western Railroad Company (hereinafter "GB&W") is a Wisconsin corporation with its principal offices in the State of Wisconsin. The individual defendants H. Weldon McGee and A. H. Schaeffer are now and have been at all times relevant hereto citizens of the State of Wisconsin. The individual defendants R. B. Wilson, John Winthrop and Charles W. Cox II are all citizens of the State of New York. Defendant Itel Corporation (hereinafter "Itel") is now and has been at all times relevant hereto a corporation incorporated under the laws of the State of Delaware with its principal offices in the State of California. This

matter exceeds, exclusive of interest and costs, the sum of $10,000.

2. The individual defendants herein are being sued by virtue of actions which arose out of their conduct as directors of GB&W and are, therefore, subject to the personal jurisdiction of the courts of the State of Wisconsin and of this court under the provisions of § 801.05(8), Stats. The defendant Itel is engaged in substantial and not isolated activities within the State of Wisconsin and is, therefore, subject to the personal jurisdiction of this court under the provision of § 801.05(1)(d), Stats.

DEFINITION OF CLASS

3. Plaintiff brings this action on behalf of himself and all holders of Class B debentures of GB&W as of November 28, 1977 similarly situated. The number of Class B debentures out-

standing as of that date was 6,376, and the plaintiff cannot, without conducting discovery, state the number of members of the class who meet the jurisdictional requirements of this Court, but plaintiff is able to state that it is impracticable to bring them all before the Court; there are questions of law and fact presented herein which are common to the entire class of persons holding Class B debentures of GB&W. The claims of the plaintiff herein are typical of the claims of the members of said class, and the plaintiff will fairly and adequately protect the interest of the class.

4. As of November 28, 1977 plaintiff was the holder of 59 of the Class B debentures of GB&W; plaintiff is presently the holder of 25 of said debentures.

CAPITAL STRUCTURE OF GB&W

5. GB&W was organized pursuant to the laws of the State of Wisconsin in 1896, in connection with a plan of reorganization of several predecessor railroads. As part of the plan of reorganization, the Articles of Incorporation provided for the issuance of certain securities as follows:

A. Two million, five hundred thousand dollars par value of instruments issued which have been known as "capital stock" in the par value of $100 each; the holders of the "capital stock" have thereafter elected the members of the Board of Directors of GB&W.

B. Six hundred thousand dollars face value of instruments issued which have been known as Class A debentures in the amount of $1,000 each. The

Articles of Incorporation provided that the Class A debentures should be repayable only:

> ". . . in the event of any sale or reorganization of the railroad and property of said company, the net proceeds thereof, after payment of all liens and charges thereon, shall be distributed to and among the holders of said Class A Debentures and the capital stock pro rata, and until such payment the holders of such Debentures shall be entitled in lieu of interest thereon to receive out of the net earnings of the railroad in each year applicable to the payment of dividends of the stock two and one-half percent (2-1/2%) upon the face value of such debentures, if earned, and after payment of two and one-half percent (2-1/2%) dividend upon the said capital stock, to participate pro rata with the stock in the net earnings of the property for each year until five percent (5%) shall have been paid upon both the stock and the said Class A Debentures, . . ."

C. Seven million dollars face value of instruments issued which have been known as Class B debentures in the amount of $1,000 each and:

> ". . . payable only in the event of a sale or reorganization of the railroad and property of said company and then only out of any net proceeds of such sale or reorganization which may remain after payment of all liens and charges upon said railroad or property, and after payment of Six Hundred Thousand Dollars ($600,000) to the holders of said Class A Debentures and Two Million Five Hundred Thousand Dollars ($2,500,000) to the stockholders, any such net proceeds remaining after such payments to be distributed pro rata to and among the holders of said Class B Debentures, the holders thereof to be entitled to receive in lieu of interest thereon any net earnings of the railroad and property in each year remaining after payment of five percent (5%) upon the said Class B Debentures and the said stock."

D. From time to time prior to November 28, 1977, GB&W had repurchased and held as treasury shares substantial amounts of the above-described securities.

6. A prior action has been concluded between representatives of the holders of Class B debentures of GB&W and its then directors, which action asserted that the directors had a duty to make certain payments to the holders of the Class B debentures and was entitled Biltchik v. Green Bay & Western R.R. Co., 250 Wis. 177 (1947). Based upon the facts litigated therein, the Court concluded that the aforesaid Class A debentures were issued to the persons who advanced new money during the course of the railroad reorganization, the "capital stock" to the holders of first mortgage bonds in foreclosure at the time of the

reorganization, and the Class B debentures to the holders of second mortgage bonds and common and preferred stock of the old company. With respect thereto, the Court held:

> "The scheme of reorganization was manifestly planned to assure that the holders of the subordinate securities should receive nothing whatever until the holders of the new Class A debentures and the new stock were compensated both through current income and on liquidation of the new corporation, and this must be borne in mind in construing the provisions of the Class B Debentures on which this suit is based" 250 Wis. at 180.

7. The Court further held, after consideration of the terms of the Class B debentures, that notwithstanding the names given to the securities in the Articles of Incorporation:

> "This as to distribution on liquidation puts the holders of the Class B Debentures on the footing

> of stockholders of an ordinary corporation. It makes them, instead of the stockholders, the owners of the equity of the corporation."

8. The Court further held that the directors of GB&W had properly exercised their discretion in refusing to make payments to the Class B debenture holders and applying the income of the corporation instead to the maintenance and improvements of the assets of the railroad and further stated:

> "The improvements made had enabled the directors to pay at least something by way of income on the Class B Debentures while prior to making such improvements there had been no net income to apply to them, and the value of the equity of the owners of the Class B Debentures had been thereby increased over $2,000,000 . . .
>
> ". . . As the earnings of the corporation were all in fact applied to proper purposes to the advantage

> of the corporation and to the advantage of the owners of Class B Debentures, no harm or prejudice resulted to the latter . . ." 250 Wis. 177-178.

9. In various other cases also involving the terms of the Class B debentures, the Courts have consistently held that the holders of the Class B debentures are, in fact, holders of the equity in GB&W and that the other securities are, in fact, debt securities. Williams v. Green Bay & Western R.R. Co., 326 U.S. 549, Sup. Ct. 284, 90 L. Ed. 311 (1946); Green Bay & Western R.R. Co. v. Commissioner, 147 F.2d 585 (7th Cir. 1945). By virtue of these decisions, the rights of the holders of the Class B debentures of GB&W are those of the holders of an equity security entitled to payment pro rata after payment of the outstanding par value of the "capital

stock" and Class A debentures of the company upon a sale of the assets of the company or a reorganization thereof as a matter of res judicata.

DUTIES OF THE DEFENDANTS

10. On November 28, 1977, the individual defendants constituted the board of directors of GB&W. The individual defendants, as directors of GB&W, owed to the holders of the Class B debentures of GB&W, who are the holders of the equity in said corporation, a duty of trust and loyalty to deal with the assets of GB&W and to manage its affairs for their benefit as fiduciaries.

11. In 1977, the defendant Itel commenced efforts to take over and control the assets and affairs of GB&W; shortly after November 28, 1977, the defendant Itel took over the management and control of GB&W, and, therefore owed

a duty of care to the holders of the Class B debentures of GB&W to manage its affairs for their benefit as a fiduciary.

THE BREACH OF DUTY

12. Prior to 1977, GB&W redeemed certain of its outstanding securities and on November 28, 1977, the following number of the three classes of securities of GB&W were outstanding and publicly held:

A. Capital stock, 18,000 shares;

B. Class A debentures, 3; and

C. Class B debentures, 6,376.

13. The individual defendants and members of their families, as of November 28, 1977, owned about 6,800 shares of capital stock of GB&W, controlled some 1,200 additional shares then held in trust and, by proxy, had control of an additional 8,000 shares.

14. Between 1974 and 1977, other railroad companies and companies engaged in railroad equipment leasing operations, including Itel, made tender offers to acquire control of GB&W, either by means of a purchase of all of the assets of GB&W or by tendering offers to acquire the securities of GB&W. The individual defendants, prior to November, 1977, had favored at least one such prior tender offer.

15. After prior negotiations, on November 28, 1977 the defendant Itel submitted an offer to the defendant directors of GB&W to purchase the assets of GB&W in an amount which would have made available to the security holders thereof a total sum of $8,500,000.

16. Upon acceptance of said offer, the proceeds of sale would have been distributable to the securities

holders of GB&W, in accordance with its Articles of Incorporation, as follows:

A. Capital stock - 18,000 shares at $100 par value, a total of $1,800,000;

B. Class A debentures - 3 at $1,000 principal amount, a total of $3,000; and

C. Class B debentures 6,376 in number, which would receive the balance of $6,697,000 or approximately $1,050 each.

17. All of said defendants knew that said offer was in the best interests of the holders of the Class B debentures of GB&W, and the individual defendants, being directors of GB&W, had a duty to the holders of the Class B debentures to obtain a distribution in said amount for their benefit.

18. The defendant directors, at the time said offer was submitted, had been informed and knew that in the event of their rejection of said offer Itel intended to submit an alternative offer to purchase the outstanding securities of GB&W, but upon payment of a greater sum to the holders of the capital stock, including themselves, but to the detriment of the holders of the Class B debentures.

19. The individual defendants breached their duty of trust and loyalty to the holders of the Class B debentures of GB&W and engaged in a course of self-dealing for the purpose of inflating the value of the shares of capital stock which they held. As a consequence of their dealings, they were able to sell the control of GB&W to Itel pursuant to said declared alternative offer and received therefrom $330 per share for the

capital stock which they held, notwithstanding the face that said capital stock had a redemption value of $100 per share.

20. Commencing on November 28, 1977 and continuing thereafter, the defendant Itel has effectuated a de facto reorganization of GB&W through its control therof [sic] in conjunction with its control over other railroads. Said defendant has not, however, as required by the Articles of Incorporation of GB&W, paid the liquidation value of the Class B debentures of GB&W to the holders thereof in the amount of $1,050, and has controlled the market for said securities at a deflated amount, offering no more than $325 for each of said Class B debentures.

DAMAGES

21. The conduct of the individual defendants and of the defendant Itel since November, 1977 has constituted

a conspiracy whereby said defendants have utilized their control over GB&W for the purpose of benefitting themselves, as holders of the capital shares of GB&W, to the detriment of the holders of the Class B debentures of GB&W. Pursuant to said conspiracy, the individual defendants and the defendant Itel have effectuated a *de facto* reorganization of GB&W and have deprived the holders of the Class B debentures thereof of their benefit in receiving their pro rata share resulting from said reorganization.

22. The plaintiff, and each other holder of Class B debentures of GB&W as of November 28, 1977 has been damaged to the extent that the plaintiff and each member of the class was deprived of the opportunity to receive the liquidation amount of $1,050 for each such debenture as of said date.

23. Since November 28, 1977, the assets of GB&W have been manipulated and wasted by the directors thereof, including the individual defendants and the directors controlled by the defendant Itel, and the acts of those in control of GB&W Have been illegal and fraudulent. Accordingly, GB&W should be liquidated either pursuant to the provisions of § 180.771(1)(a)2. and 3., Stats., pursuant to the Articles of Incorporation, or pursuant to the general equity powers of this Court and the assets applied in payment of the claims of the Class B debenture holders as of November 28, 1977.

WHEREFORE, plaintiff prays for relief as follows:

1. That an order be entered herein allowing this action to be maintained as a class action under the pro-

visions of Rule 23 of the Federal Rules of Civil Procedure by plaintiff on behalf of himself and on behalf of all holders of Class B debentures of the defendant Green Bay and Western Railroad Company as of November 28, 1977.

2. That judgment be entered in favor of said class and against the defendants H. Weldon McGee, A. H. Schaeffer, R. B. Wilson, John Winthrop, Charles W. Cox II and Itel Corporation in the sum of $6,697,000 together with interest since November 28, 1977. That said judgment further provide that the assets of the defendant Green Bay and Western Railroad Company be liquidated to the extent necessary to create a fund in that amount.

3. That the defendants be held jointly and severally further liable for the costs and expenses of this action.

4. That the fund created as a result of the judgment entered in this Court be administered by the Court and such further orders be entered providing for the payment from said fund for the costs and expenses of this litigation and to the holders of the Class B debentures of the Green Bay and Western Railroad Company since November 28, 1977 as their respective interests may appear.

Robert K. Steuer and
William J. Mantyh,
Attorneys for Plaintiff

By: ____________________
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TOK6:E

AMENDED ANSWER

(<u>Eliasen</u> case)

UNITED STATES DISTRICT COURT FOR
THE EASTERN DISTRICT OF WISCONSIN

AXEL N. ELIASEN, on behalf of himself and all others similarly situated,

Plaintiff,

v.

GREEN BAY & WESTERN RAILROAD COMPANY, H. WELDON McGEE, R. B. WILSON, JOHN WINTHROP and CHARLES W. COX II

Defendants.

Civil Action No. 80-C-1092

AMENDED ANSWER OF GREEN BAY & WESTERN RAILROAD COMPANY

Defendant Green Bay & Western Railroad Company (GBW), by its attorneys Quarles & Brady, for its answer to the Amended Complaint herein:

1. Lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation

that the plaintiff is now and was at all times relevant hereto a citizen of the State of Illinois, admits that GBW is a Wisconsin corporation with its principal offices in the State of Wisconsin, lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation that the individual defendants H. Weldon McGee and A. H. Schaeffer are now and have been at all times relevant hereto citizens of the State of Wisconsin, lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation that the individual defendants R. B. Wilson, John Winthrop and Charles W. Cox II are all citizens of the State of New York, admits that defendant Itel Corporation is now and has been at all times relevant hereto a corporation incorporated under the laws of the State

of Delaware with its principal offices in the State of California, and denies each and every other allegation of paragraph 1.

2. Admits that plaintiff purports to be suing the individual defendants because of actions which arose out of their conduct as directors of GBW, admits the existence of Wis. Stat. §801.05(8), lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation that the individual defendants are subject to the personal jurisdiction of the courts of the State of Wisconsin and of this court, lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation that the defendant Itel is engaged in substantial and not isolated activities within the State of Wisconsin, lacks

knowledge or information sufficient to form a belief as to the truth and accuracy of the allegation that Itel is therefore subject to the personal jurisdiction of this court under the provisions of Wis. Stat. §801.05(1)(d), admits the existence of Wis. Stat. §801.05(1)(d), and denies each and every other allegation of paragraph 2.

3. Admits that plaintiff purports to bring this action on behalf of himself and all holders of Class B Debentures of GBW as of November 28, 1977, similarly situated, admits that the number of Class B Debentures outstanding as of that date was 6,376, and lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the remaining allegations of paragraph 3.

4. Lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the allegations of paragraph 4.

5. Denies the allegation that from time to time prior to November 28, 1977, GBW had repurchased and held as treasury shares substantial amounts of Class A or Class B Debentures, affirmatively alleges that the word "shares" is inappropriate to describe the Class B Debentures, and admits the remaining allegations of paragraph 5.

6. Admits the existence of Biltchik v. Green Bay & Western Railroad Company, 250 Wis. 177 (1947) and the accuracy of the quotation therefrom; but insofar as any facts are alleged, denies each and every other allegation of paragraph 6, and affirmatively alleges on information and belief that the Class B

Debentures were issued to the holders of income bonds, common stock and preferred stock of the old company.

7. Admits the existence of the Biltchik case and the accuracy of the quotation therefrom; but insofar as any facts are alleged, denies each and every other allegation of paragraph 7, and affirmatively alleges on information and belief that since 1896 the Class B Debentures have been treated as debt instruments, transactions in Class B Debentures are not recorded, Class B debentures are not registered, holders of Class B debentures never have been allowed to vote or attend shareholders meetings, and holders of Class B debentures have never been accorded the right to inspect the corporate books and records.

8. Admits the existence of the Biltchik case and the accuracy of the

quotations therefrom; but insofar as any facts are alleged, denies each and every other allegation of paragraph 8.

9. Admits that the holders of the Class B debentures of GBW are entitled to payment pro rata after payment of the outstanding par value of the capital stock and Class A debentures of the GBW upon a sale of the assets of the GBW or a reorganization thereof; denies each and every other allegation of paragraph 9; and affirmatively alleges that the holders of Class B debentures are entitled to no more than $1,000 per $1,000 face value of debenture.upon the sale of the assets or a reorganization of GBW.

10. Admits that on November 28, 1977, the individual defendants were Directors of GBW, and denies each and every other allegation of paragraph 10.

11. Admits that in 1977, Itel commenced efforts to acquire a controlling interest in GBW, admits that after November 28, 1977, Itel purchased approximately 99% of the outstanding common stock of GBW, admits that this purchase of a 99% interest in the common stock of GBW gives Itel some measure of control over GBW, and denies each and every other allegation of paragraph 11.

12. Admits the allegations of paragraph 12.

13. Admits that the individual defendants, as of November 28, 1977, owned 5,344 shares of GBW common stock, admits that 2,660 shares of GBW common stock were held by members of families of the individual defendants or held in trust, making a total of 8,004 shares of GBW common stock owned or controlled to some extent by the individual defendants,

and lacks knowledge or information sufficient to form a belief as to the truth and accuracy of the remaining allegations of paragraph 13.

14. Admits that beween 1974 and 1977, other railroad companies and companies engaged in railroad equipment leasing operations, including Itel, made tender offers to acquire control of GBW by tendering offers to acquire the securities of GBW, admits that the GBW Board of Directors, prior to November, 1977, had favored at least one such prior tender offer, and denies the remaining allegations of paragraph 14.

15. Denies each and every allegation of paragraph 15.

16. Denies each and every allegation of paragraph 16.

17. Denies each and every allegation of paragraph 17.

18. Denies each and every allegation of paragraph 18.

19. Admits that Itel made a tender offer in an attempt to purchase a controlling amount of GBW common stock, admits that the holders of GBW common stock received $330 per share for the common stock which they held, if they tendered it in response to the Itel tender offer, admits that the common stock had a par value of $100 per share, and denies each and every other allegation of paragraph 19.

20. Admits that Itel has offered no more than $325 for each Class B debenture, and denies each and every other allegation of paragraph 20.

21. Denies each and every allegation of paragraph 21.

22. Denies each and every allegation of paragraph 22.

23. Denies each and every allegation of paragraph 23.

DEFENSE

1. The Amended Complaint fails to state a claim upon which relief can be granted against defendant GBW. There are no well-pleaded facts in the Amended Complaint which, taken as true for the purposes of this defense only, could support the entering of any relief as against defendant GBW.

AFFIRMATIVE DEFENSE

The rights of the holders of Class B debentures of GBW have been determined in a previous litigation entitled Biltchik v. Green Bay & Western Railroad Company, 250 Wis. 177 (1947). As a matter of res judicata, the holders of Class B debentures are entitled to no more than $1,000 per $1,000 face value of debentures upon the sale of the assets or a reorganization of GBW.

PRAYER FOR RELIEF

1. That the prayer of plaintiff that an order be entered allowing this action to be maintained as a class action be denied;

2. That the Amended Complaint be dismissed, on the merits, with prejudice, and an order be entered awarding defendant GBW its full costs, disbursements, expenses and attorneys fees incurred in answering the Amended Complaint;

3. That if this Court should find that any holder of Class B debentures should recover in this action, this Court should also find that the amount a holder of Class B debentures of GBW could recover upon a sale or reorganization of GBW is limited to $1,000 per $1,000 face value of debenture;

4. That defendant GBW be awarded its costs and attorneys fees pursuant to Wis. Stat. §814.025(1), and that such award be taxed to the plaintiff, his attorneys or both, as the Court deems just, pursuant to Wis. Stat. §814.025(2); and

5. That defendant GBW be awarded such other and further relief as may be appropriate.

Dated this 7th day of August, 1981.

THOMAS O. KLOEHN
CHARLES A. GRUBE

Attorneys for Defendant
Green Bay & Western
Railroad Company

Of Counsel:

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(414) 277-5000

Direct Inquiries To:

Thomas O. Kloehn
(414) 277-5000

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Amended Answer of Green Bay & Western Railroad Company was this date served upon the plaintiff by mailing a copy thereof to the attorney for the plaintiff, postage prepaid, at his last known address, to wit:

Robert K. Steuer, Esq.
Weiss, Steuer, Berzowski,
Brady & Donohue
Suite 1500
700 North Water Street
Milwaukee WI 53202

Dated this 7th day of August, 1981.

____
Charles A. Grube

TOK6:D

CASE NO. 83-27

RECEIVED
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SUPREME COURT, U.S.

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1983

AXEL N. ELIASEN, on behalf of himself
and all others similarly situated,

Petitioner,

v.

GREEN BAY & WESTERN RAILROAD COMPANY,
H. WELDON McGEE, R. B. WILSON, JOHN
WINTHROP, and CHARLES W. COX, II,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

RESPONDENTS' MOTION FOR
AN AWARD OF DAMAGES
PURSUANT TO SUPREME COURT RULE 49.2

Thomas O. Kloehn
780 North Water Street
Milwaukee WI 53202
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Counsel for Respondents

Of Counsel:
Charles A. Grube
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MOTION

Respondents Green Bay & Western Railroad Company, H. Weldon McGee, R. B. Wilson, John Winthrop, and Charles W. Cox, II, by their attorneys, hereby move this Court for an award of appropriate damages for the reason that the Petition for a Writ of Certiorari filed in this case is frivolous. This Motion is expressly based upon Supreme Court Rule 49.2.

ARGUMENT

Respondents have shown the Court in their brief in opposition to the petition for certiorari why the petitioner's contentions are frivolous. This case does not even colorably fit the requirements of Supreme Court Rule 17 governing review on certiorari, nor does it raise any important question of law or fact.

Respondents have been damaged by being forced to incur attorneys fees and expenses in responding to the petition for certiorari. Respondents, therefore, request this Court to order petitioner to pay respondents the sum of $5,000.00 as appropriate damages.

Dated this 10th day of August, 1983.

Respectfully submitted,

Thomas O. Kloehn

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